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The Manufacturers
Hanover
Financial
Digest

Weekly Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, NOVEMBER 4, 1985
VOLUME XXII, NUMBER 39

Japan In The Fast Lane . . .

Last year, Japan and four neighboring economies in East Asia—Hong Kong, Singapore, South Korea and Taiwan—posted some of the world's fastest economic growth rates. This is a distinction they have enjoyed for several decades. However, only Japan among them is doing at least as well this year. This is because the other countries, experiencing slower export growth and troubled by certain internal weaknesses, are growing at much slower rates and registering much smaller improvements in their external payments balances than previously recorded.

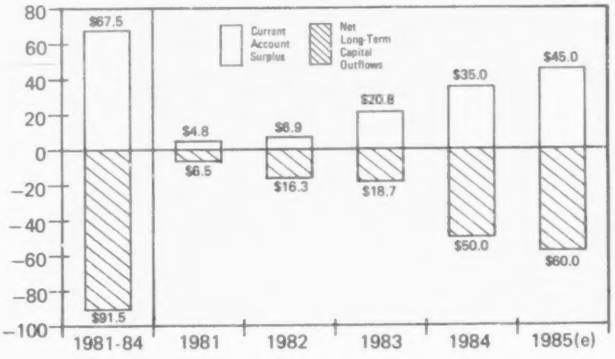
For Japan, however, this is not the case. With domestic spending firming, the pace of business activity remains robust. Overall real gross national product growth this year is expected to be in the same 5½ percent neighborhood as last year. And with export sales of such products as automobiles and video cassette recorders strong, especially those destined for the vast U.S. market, Japan's trade and current account surpluses show no sign of narrowing. Indeed, just the opposite is occurring with the trade surplus continuing to widen and the current account surplus likely to reach another record for the third straight year. The current account surplus ran at a nearly $43 billion annual clip during the first eight months of 1985 and could reach $45 billion for the year as a whole. If these numbers hold, it would mark the largest current account surplus ever posted by any country.

Not surprising, the financial surplus stemming from Japan's export success is now approaching proportions similar to those generated by OPEC during the days of soaring oil prices. And, as with oil exporters, Japan finds itself recycling an ever larger volume of funds back into the world's financial markets. Last year alone, net long-term capital outflows reached nearly $50 billion, an amount larger than in the immediately preceding three years put together (see chart). Half of this was channeled into the world's bond markets. With this year's surplus running some 20 percent larger than last year's, Japan will remain both a major exporter of goods and services worldwide, as well as a dominant exporter of capital. Where will the money go? One good bet is the United States, where long-term interest rates still exceed those in Japan by about four full percentage points.

. . . Passing Other Asian Economies . . .

The poorer performance of the other major East Asian economies reflects in part the occasionally adverse side effects arising from a strong reliance on exports to fuel domestic business activity. Merchandise exports in these countries, excluding re-exports, comprise a larger proportion of gross national product than in Japan—ranging from as high as 85 percent in Singapore to as "low" as 35 percent in South Korea. This compares with less than 14 percent in Japan and six percent in the United States. As a result, when world export markets are strong, these countries often grow at rates even more rapid than that of Japan. But when these markets weaken, growth in these smaller East Asian countries often fades faster.

JAPAN:
CURRENT ACCOUNT SURPLUSES VS. NET LONG-TERM CAPITAL OUTFLOWS
(BILLIONS OF U.S. DOLLARS)



The United States in particular looms large as an export market for these countries. Last year, sales to the United States accounted for nearly half of Taiwan's and Hong Kong's exports, a third of Korea's and a fifth of those of Singapore. With exports to the United States sparking growth throughout the region, real GNP growth reached 7½ percent in South Korea, eight percent plus in Singapore, 9½ percent in Hong Kong and almost 11 percent in Taiwan.

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But the reverse is now underway. With U.S. imports growing more slowly this year than last year, growth in East Asia has begun to slow. For the first nine months of this year, despite their sharp rise in September, U.S. imports are up only four percent compared with the same period a year ago, and the growth of imports from Korea, Taiwan and Singapore are now much lower than a year ago. What is more, in light of the continuing sluggishness of economic activity in Europe and in the other advanced developing countries, this slack has not been offset anywhere else. As a result, this year's real economic growth rates will be sharply reduced, ranging from no growth in Singapore, to about three to five percent for Taiwan, Hong Kong and South Korea.

. . . That Have Shifted Into Lower Gear

Some internal economic weaknesses are also contributing to the current business downturn. These include undue emphasis on either a narrow export product line or product lines experiencing stagnant demand at best. Hong Kong, for example, still relies upon textiles and apparel for around 40 percent of its export revenues, while Taiwan is in a similar, highly concentrated position. Meanwhile, South Korea depends upon just three industries—shipbuilding, footwear and textiles and apparel—for nearly 50 percent of export revenues.

Several of Singapore's major exports are finding

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 10/30/85	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	176.982	– 2.385	+19.046
Loans to Depository Inst.	1.025	– .276	– 4.162
Float	.549	– .320	– .008
Total Reserve Bank Credit	193.065	– 2.503	+16.906
Treasury Deposits with Federal Reserve Banks	2.664	– .986	– 1.139
Currency in Circulation	188.540	– .880	+12.683
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	123.327	+ .418	+ 4.094
	10/23/85		
Member Bank Reserves:			
Total Reserves Held	43.803	+ .025	+ 5.960
Excess (Deficiency)	.802	+ .140	+ .386
Net Free Reserves	.333	+ .439	+ .720
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates†			
M1 (10/21/85)	613.6	+ 11.0‡	+ 11.4‡
M2 (September '85)	2,528.4	+ 9.0	+ 9.5
M3 (September '85)	3,163.3	+ 7.8	+ 9.0
Domestic Nonfinancial Debt (2nd Q'85)	6,317.3	+ 12.2	+ 13.6

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 11/1/85	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	7.19%	7.27%	7.35%
* Federal Agencies	8.43	8.69	9.10
* Municipal Notes—High Grade (46% Taxable Equivalent)	8.15	8.70	9.72
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.75	7.75	8.10

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	7.85%	Dec.	7.85%
15- 29 days	7.85	Jan.	7.80
30- 59 days	7.80	Feb.	7.80
60- 89 days	7.75	Mar.	7.80
90-179 days	7.68	Apr.	7.80
180-239 days	7.65	May	7.80
240-270 days	7.65		

‡ Industrial Paper—Prime			
30- 89 days	7.78%	†Federal Funds Effective Rate	8.40%
90-120 days	7.70		

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 3,916	$ 3,853	$ 3,695
Gross National Product (1972 Dollars)*	3rd Q'85	$ 1,685	$ 1,671	$ 1,645
Percent Change, Annual Rate	3rd Q'85	3.3	1.9	1.6
Change in Consumer Prices*	Sep '85	2.4%	2.4%	4.8%
Change in Producer Prices*	Sep '85	– 7.2%	– 3.6%	0.0%
Civilian Employment (Thousands of Persons)†	Oct '85n	107,867	107,544	105,649
Unemployment as % of Civilian Labor Force†	Oct '85n	7.1%	7.1%	7.3%
Personal Income*	Sep '85	$ 3,209	$ 3,199	$ 3,068
Leading Indicators Composite Index (1967=100)†	Sep '85n	170.3	170.2r	165.7
Industrial Production Index (1977=100) †	Sep '85	124.7	124.8	123.3
Net Change in Consumer Installment Credit †	Aug '85	$ 6.31	$ 6.25	$ 6.02
U.S. Merchandise Trade Balance †	Sep '85n	–$ 15.55	–$ 9.90	–$ 11.54
Plant and Equipment Expenditures*	4th Q'85	$387.40(a)	$389.54(a)	$368.29
Private Housing Starts (Thousands of Units)*	Sep '85	1,583	1,746	1,669
New Construction Expenditures*	Sep '85n	$ 350.4	$ 343.9r	$ 321.0
Total Business Inventories †	Aug '85	$ 577.9	$ 580.1	$ 561.7
Total Business Sales †	Aug '85	$ 429.1	$ 422.5	$ 413.3

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

buyers few and far between at this time. Exports of computer-related products and of shipping services are suffering from the severe global slump in these industries. The important oil-refining and offshore oil-drilling industries are also depressed. Many of Singapore's former clients now refine their own oil, and Saudi Arabia, which is beginning to export refinery products in the region, is giving the country new and substantial competition.

So, too, protectionism in the industrial world is a threat which East Asia will increasingly have to face. Shipments of textiles from these and other developing countries are already restricted under international agreements. Shipments of steel and television sets from South Korea to the United States are also restrained under other arrangements. Exports of shoes, important to both Korea and Taiwan, are the current targets of protectionist legislation in the United States.

But despite such problems, the long-term economic potential of these countries remains bright. This is because of their high savings rates, strong emphasis on exports, openness to foreign investment and generally pro-business government policies. Add to this generally favorable external debt profiles, and a recipe is in place for further economic success.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since	
		Week Ago	Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (10/16/85)	157,090	– 1,639	– 3,789
New York City (10/23/85)	33,649	+ 229	– 529
Commercial Paper (10/23/85)	286,404	+ 1,830	+54,490

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since	
		Week Ago	Year Ago
Nationwide (10/16/85)	252,077	– 864	+ 4,813
New York City (10/23/85)	59,525	– 422	– 4,763

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since	
		Week Ago	Year Ago
Nationwide (10/16/85)	691,890	– 798	+ 59,145
New York City (10/23/85)	149,922	– 2,502	+ 8,627

Financial Markets

	Friday 11/1/85	Change Since	
		Week Ago	Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.44%	+ .21	– 1.84
180-Day Bills†	7.68	+ .27	– 2.03
Longest Bills†	7.91	+ .42	– 2.18
Recent Issues:			
10s 10/31/87	8.70	– .16	
$9^{3}/_{8}$s 9/30/89	9.24	NA	
$10^{1}/_{2}$s 8/15/95	9.98	– .21	
$10^{5}/_{8}$s 8/15/15	10.25	– .22	
Municipals:			
Bond Buyer–20 Bond Index* (10/31/85)	8.76%	– .19	– 1.35
Blue List Total ($ Million)	$1,424	–$ 282	– $ 441
30-Day Visible Supply ($ Million)	$5,879	+$1,518	+ $4,102
Total	$7,303	+$1,236	+ $3,661
Corporates:			
Moody's Aa Composite (10/31/85)	11.31%	– .09	– 1.47
30-Day Visible Supply ($ Million)	$3,023	+$1,178	+ $1,288
Stocks:			
Dow-Jones Averages:			
Industrials	1,390.25	+ 33.73	+ 173.60
Transportation	665.61	+ 16.03	+ 133.29
Utilities	161.78	+ 2.62	– 17.96
65 Stocks	563.19	+ 13.06	+ 80.98
Standard and Poor's 500 Stocks	191.53	+ 4.01	+ 24.11
N.Y.S.E. Composite Index	110.55	+ 2.19	+ 14.04
N.Y.S.E. Avg. Daily Vol. for Week (000's)	116,058	+ 5,246	+ 24,996

* 46% Taxable equivalent 16.22%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 11/1/85	Week Ago
Overnight	8.19%	7.81%
1 month	7.94	8.06
3 month	8.00	8.13
6 month	8.00	8.25
1 year	8.25	8.56
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.90%	10.00%
Long Term (7 to 15 yrs.)	10.40	10.50

FOREIGN EXCHANGE SPOT RATES

New York Opening (11/1/85)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.01893	52.8300
Canada	.7312	1.3676
Denmark	.1059	9.4450
France	.1259	7.9425
Germany	.3835	2.6075
Italy	.0005674	1762.50
Japan	.004769	209.70
Mexico	.002090	478.50
Netherlands	.3401	2.9403
Switzerland	.4669	2.1418
U.K.	1.4380	.6954

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A Leader in Public Finance

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Corporate Finance and Investment Management Leadership

We draw on the traditional corporate finance skills of our experienced officer staff, as well as the depth of our customer base, to be a leader in structuring mergers and acquisitions, buyouts, project finance and venture capital.

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The Manufacturers Hanover Financial Digest

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and Business Indicators

FRIDAY, NOVEMBER 8, 1985
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Spotlight Focuses On The Consumer . . .

The consumer sector has received much attention recently and with good reason. Accounting for two-thirds of our gross national product, sales of goods and services to individuals and families far surpass the other two major domestic purchasers, business and government. Moreover, while real GNP has increased at an annual rate of only 1.8 percent during the first three quarters of this year, real personal consumption expenditures have climbed by a healthier 4.9 percent annual rate. Now with the start of the important Holiday shopping season less than three weeks away, concern is mounting that the consumer is tapped out.

To be sure, on the surface, household finances seem to be in trouble. Consumer credit compared with disposable income is at a record 18.9 percent, income growth has slowed, and the savings rate—savings as a percent of disposable income—is now 1.9 percent—the lowest rate in at least 35 years. However, as has been pointed out in the past (Financial Digest—September 23, 1985), the aggregate figures mask a more positive picture underneath. For example, much of the debt accumulated has been taken on by those high-income households which are probably best able to service it. And while the low savings rate has received notoriety in the press, the savings number may be somewhat misleading. This is because different government agencies use different methods to estimate personal savings levels.

. . . But A Misleading Savings Rate . . .

The savings rate most quoted in the press uses a savings level calculated by the Commerce Department. This method takes monthly disposable incomes and subtracts consumption expenditures, interest paid by consumers to businesses and any transfer payments to people abroad, leaving a residual assumed to be savings. This approach has resulted in the 1.9 percent rate in September, down from the 2.9 percent average of the third quarter, and the 5.1 percent average for the second quarter.

The Federal Reserve, on the other hand, looks at the quarterly increases in households' financial and certain tangible assets then subtracts the changes in debt, contributions to government insurance and pension funds, and depreciation. The final number as a percent of disposable income gives a savings rate for the second quarter (the latest available) of 6.3 percent. The gap between the two different savings figures has varied in the past by tens of billions of dollars, obviously causing divergencies in the two savings rates.

Studies have shown that some of the major differences between the two calculations include such items as unrecorded capital flows from abroad, the effects of the underground economy on incomes and the understatement of domestic investment. However, another distinction causing the recent downward shift in the Commerce Department's savings rate is that this method does not take into account the accumulation of debt when purchases are made. For instance, in computing personal consumption expenditures, the total dollar amount of new cars sold is included, although only 25 percent of all new cars sold are paid for in full at the time of the purchase. The other 75 percent are bought on credit.

This becomes important in light of the strong sales of new cars in August and September. Low financing rates caused extraordinary jumps in sales, about 1.8 million units at an annual rate above the recent trend for August and 3.7 million units higher in September. If these extraordinary increases in car sales are excluded, the savings rates in August and September would probably have been 3.6 percent and 3.3 percent, respectively—not far from the 3.7 percent and 3.8 percent rates in June and July. Moreover, if the total dollar amount spent on all new cars that was obtained through financing is taken out of consumption expenditures, the savings rate for August and September would jump to 6.5 and 6.1 percent, respectively.

. . . Overshadows More Positive Signs

No question, consumers have led the U.S. economy down the road of the current business expansion. In particular, over the past three quarters, the economy's lackluster performance might well have developed into a full-fledged recession, were it not

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for consumers' willingness to spend. Consumer spending, adjusted for inflation, has increased more than 14 percent during this expansion—almost two percentage points higher than the average rise in real consumption over the same time span of most other postwar recoveries. In fact, only in the 1975-79 expansion did consumers increase their spending faster than today. However, the stepped-up spending seen in the late 1970s was a result of a "buy now before prices go up" psychology in which consumers went off on a buying and borrowing binge in order to protect themselves against that period's rapid escalation of prices.

In today's low inflation environment, it seems that the most important determinant of consumer spending is the employment situation. Although the civilian unemployment rate in October was unchanged from September's 7.1 percent of the labor force, a substantial gain in employment did take place. Nonfarm businesses added 415,000 jobs to their payrolls. What is more, the gains in wage and salary employment were widespread, with more than two-thirds of the 185 industries monitored by the Bureau of Labor Statistics registering increases. Even the manufacturing sector, battered by foreign competition, added 60,000 workers to its payrolls after posting declines throughout most of 1985.

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 11/6/85	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	178.838	+ 1.856	+17.767
Loans to Depository Inst.	1.125	+ .100	− 4.436
Float	.417	− .132	+ .204
Total Reserve Bank Credit	195.158	+ 2.093	+15.743
Treasury Deposits with Federal Reserve Banks	3.107	+ .443	− .084
Currency in Circulation	189.880	+ 1.340	+12.881
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	126.296	+ 2.969	+ 7.929
	11/6/85		
Member Bank Reserves:			
Total Reserves Held	43.580	− .239	+ 5.585
Excess (Deficiency)	.790	− .028	+ .224
Net Free Reserves	.313	− .036	+ .936
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates †			
M1 (10/28/85)	611.4	+ 10.3‡	+ 11.4‡
M2 (September '85)	2,528.5	+ 9.0	+ 9.5
M3 (September '85)	3,164.1	+ 7.9	+ 9.1
Domestic Nonfinancial Debt (2nd Q'85)	6,317.3	+ 12.2	+ 13.6

†Seasonally adjusted.

* Seasonally adjusted annual rate.

‡ Four-week moving average.

New York Money Market

Offering Rates 11/8/85	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	7.27%	7.31%	7.33%
* Federal Agencies	8.35	8.50	9.00
* Municipal Notes—High Grade (46% Taxable Equivalent)	8.33	8.56	9.49
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.78	7.78	7.95

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	7.80%	Dec.	7.77%
15- 29 days	7.90	Jan.	7.72
30- 59 days	7.80	Feb.	7.67
60- 89 days	7.75	Mar.	7.64
90-179 days	7.70	Apr.	7.62
180-239 days	7.65	May	7.57
240-270 days	7.65		

‡Industrial Paper—Prime		†Federal Funds	
30- 89 days	7.78%		
90-120 days	7.70	Effective Rate	7.85%

‡Discount basis.

* Subject to availability.

† Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

		Latest Period or End of Period	Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 3,916	$ 3,853	$ 3,695
Gross National Product (1972 Dollars)*	3rd Q'85	$ 1,685	$ 1,671	$ 1,645
Percent Change, Annual Rate	3rd Q'85	3.3	1.9	1.6
Change in Consumer Prices*	Sep '85	2.4%	2.4%	4.8%
Change in Producer Prices*	Sep '85	− 7.2%	− 3.6%	0.0%
Civilian Employment (Thousands of Persons) †	Oct '85	107,867	107,544	105,649
Unemployment as % of Civilian Labor Force †	Oct '85	7.1%	7.1%	7.3%
Personal Income*	Sep '85	$ 3,209	$ 3,199	$ 3,068
Leading Indicators Composite Index (1967=100) †	Sep '85	170.3	170.2	165.7
Industrial Production Index (1977=100) †	Sep '85	124.7	124.8	123.3
Net Change in Consumer installment Credit †	Aug '85	$ 6.31	$ 6.25	$ 6.02
U.S. Merchandise Trade Balance †	Sep '85	−$ 15.55	−$ 9.90	−$ 11.54
Plant and Equipment Expenditures*	4th Q'85	$387.40(a)	$389.54(a)	$368.29
Private Housing Starts (Thousands of Units)*	Sep '85	1,583	1,746	1,669
New Construction Expenditures*	Sep '85	$ 350.4	$ 343.9	$ 321.0
Total Business Inventories †	Aug '85	$ 577.9	$ 580.1	$ 561.7
Total Business Sales †	Aug '85	$ 429.1	$ 422.5	$ 413.3

*Seasonally adjusted annual rate.

†Seasonally adjusted.

n-Newly reported figure.

r-Revised.

a-Anticipated.

Not only is total employment at record levels, but the employment rate—the number of people holding jobs as a percent of the population over 16 years old—now matches its record mark attained last March. At 60.3 percent in October, the employment rate is three percentage points higher than its postwar average. Future employment prospects still remain bright. The Conference Board reports that the volume of help-wanted advertising in U.S. newspapers—a harbinger of additional hiring prospects—rose in the latest month.

Consumer attitudes seem to be brightening just in time for Holiday buying. According to the Conference Board's latest survey, consumer confidence in October rose after two months of declines. Although fewer people now plan to buy cars, which comes as no surprise in view of record auto purchases in August and September and the expiration of most cut-rate financing, consumers now feel it's time to step up spending on such major home appliances as television sets, vacuum cleaners, washing machines and dryers. The number of people who in October planned to buy such appliances reached the highest level in seven years. As long as employment continues to rise bringing increased incomes and security, consumers should be less prone to tighten their purse strings or lock up their credit cards—good news for merchants as they plan for the approaching Holiday shopping season.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (10/23/85)	157,350	+ 268	– 4,042
New York City (10/30/85)	33,764	+ 115	– 71
Commercial Paper (10/30/85)	286,048	– 356	+55,499

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (10/23/85)	252,506	+ 444	+ 4,747
New York City (10/30/85)	59,665	+ 140	– 4,356

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (10/23/85)	687,723	– 4,325	+ 52,237
New York City (10/30/85)	152,047	+ 2,132	+ 8,906

Financial Markets

	Friday 11/8/85	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.46%	+ .02	– 1.54
180-Day Bills†	7.64	– .04	– 1.87
Longest Bills†	7.80	– .11	– 2.17
Recent Issues:			
10s 10/31/87	8.56	– .14	
$9^{3}/_{8}$s 9/30/89	9.11	– .13	
$10^{1}/_{2}$s 8/15/95	9.84	– .14	
$10^{5}/_{8}$s 8/15/15	10.14	– .11	
Municipals:			
Bond Buyer–20 Bond Index* (11/7/85)	8.68%	– .08	– 1.49
Blue List Total ($ Million)	$1,578	+$ 154	– $ 154
30-Day Visible Supply ($ Million)	$8,098	+$2,219	+ $4,648
Total	$9,676	+$2,373	+ $4,494
Corporates:			
Moody's Aa Composite (11/7/85)	11.18%	– .13	– 1.60
30-Day Visible Supply ($ Million)	$1,868	–$1,155	– $3,139
Stocks:			
Dow-Jones Averages:			
Industrials	1,404.36	+ 14.11	+ 185.39
Transportation	678.14	+ 12.53	+ 145.71
Utilities	161.93	+ .15	+ 16.16
65 Stocks	569.44	+ 6.25	+ 85.69
Standard and Poor's 500 Stocks	193.72	+ 2.19	+ 26.12
N.Y.S.E. Composite Index	111.95	+ 1.40	+ 15.22
N.Y.S.E. Avg. Daily Vol. for Week (000's)	117,604	+ 1,546	+ 23.658

* 46% Taxable equivalent 16.07%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 11/8/85	Week Ago
Overnight	7.81%	8.19%
1 month	8.00	7.94
3 month	8.06	8.00
6 month	8.06	8.00
1 year	8.25	8.25
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.80%	9.90%
Long Term (7 to 15 yrs.)	10.35	10.40

FOREIGN EXCHANGE SPOT RATES

New York Opening (11/8/85)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.01886	53.03
Canada	.7261	1.3773
Denmark	.1054	9.4875
France	.1251	7.9925
Germany	.3812	2.6233
Italy	.0005651	1769.50
Japan	.004861	205.70
Mexico	.002083	480.00
Netherlands	.3381	2.9575
Switzerland	.4638	2.1560
U.K.	1.4160	.7062

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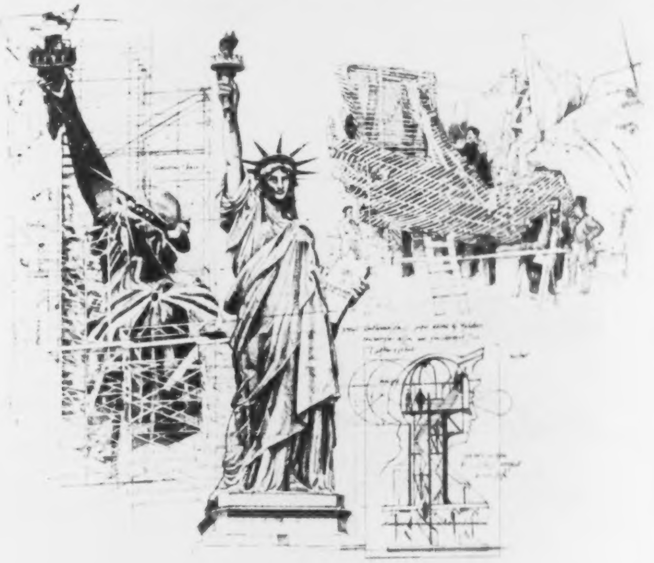

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The Manufacturers Hanover Financial Digest
Weekly Commentary, Selected Financial Data, and Business Indicators

MONDAY, NOVEMBER 18, 1985
VOLUME XXII, NUMBER 41

Free Trade Between The U.S. And Canada . . .

With each passing month of skyrocketing trade deficits, protectionism has become an urgent topic in boardrooms, factories, union halls and Congress alike. But despite talk of erecting more barriers in the United States against foreign goods, the opposite attitude toward imports prevails in Canada. There, discussions are now underway concerning a possible treaty dismantling many of the restrictions on trade between the United States and Canada. Official negotiations may begin next year leading to a free trade agreement between these two countries.

Free trade would be very much in keeping with the strong U.S.-Canada bilateral relationship which through the years has been moving steadily, if undramatically toward greater coordination and harmonization. This is evident in the closely linked capital markets of the two countries, extensive cross-border investment, abundant social and cultural linkages, and the frequent, unfettered movement of people across a common border.

A free trade agreement has been mentioned intermittently by the governments of both countries since the late 1970s. However, it was not until March of this year at a meeting between President Reagan and Prime Minister Mulroney that a commitment was first made to pursue the idea actively. In fact, such industries as automobiles and defense already have trade agreements promoting greater efficiency for both countries through an integrated North American market.

The importance of the Canadian trade relationship cannot be overstated. Canada is by far our largest trading partner, accounting for about 20 percent of both U.S. imports and exports. Our exports to Canada are not only twice as large as our exports to Japan or to Latin America, but even larger than U.S. exports to the entire European Economic Community. The United States and Canada have the largest two-way trade relationship in the world, estimated at about $125 billion this year.

In recent years, the United States has usually run a surplus on services—tourism, interest and dividend income—and a deficit on merchandise trade. The vigorous U.S. business expansion of the past three years has caused our merchandise trade deficit with Canada to accelerate rapidly. But special factors also contributed to this deficit. Canadian automotive exports benefited not only from the strong upturn in the U.S. auto market, but also from U.S. consumers' preferences once again for larger cars—a Canadian specialty.

Canada also enjoys a sizable surplus in the trading of petroleum and natural gas. Not only has Canadian production been increasing recently, but their domestic prices have gradually moved towards world levels, discouraging domestic demand and making more fuel available for exports. As a result, Canada trails only Mexico as the most important supplier of fuel to the United States—not to mention one of the most dependable.

. . . Can Benefit Both Countries . . .

The strong U.S. business expansion and its accompanying demand for imports have given a solid boost to Canadian economic growth. Exports make up over one fourth of Canadian GNP, and about three quarters of these exports are destined for the United States. In turn, stepped-up Canadian economic growth positively affected Canadian demand for U.S. goods. Paced by increased shipments of automotive parts, U.S. sales to Canada rose 22 percent last year—reaching $46.5 billion and providing jobs for an estimated 1.1 million U.S. workers—a fact too often forgotten in the talk of jobs lost because of U.S. imports from other countries.

Building on the already close trading ties which have benefited both the U.S. and Canada, an enhanced trade agreement will further strengthen this positive relationship. For the U.S., this will mean greater access to the markets of a country whose present tariffs are among the highest in the industrialized world. U.S. exports to Canada face an average 9.4 percent tariff, while the U.S. average rate is only 4.7 percent. In the present environment of a strong U.S. dollar and growing protectionist sentiment in other industrialized countries, the U.S. stands to gain from any development which would expand our market.

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For Canada, on the other hand, the benefits from a more open trade door are different—and possibly more substantial. For one thing, the small size of their domestic market is often cited as a major brake on Canada's growth prospects. Canada's 25 million people—approximately one ninth as large as America's population—are disbursed over an area slightly larger than the U.S. In fact, Canada is the only advanced industrial country which does not have direct access to a market of over 100 million people.

The small size of the domestic market has prevented Canadian industry from enjoying economies of scale, and attempts to replicate the wide range of products available in the much larger U.S. market have fostered fragmentation and inefficiency. What is more, since the 1870s Canada has had a strategy of high-tariff protectionism which has also led to inefficiency in many industrial sectors. Trade liberalization and extended access to larger markets will challenge Canadian industries to become more efficient while providing a chance for industrial specialization, economies of scale and higher productivity.

Freeing trade is also important to Canada in light of today's relatively low inflation environment in general, and the softening of raw materials prices in particular. Canada is no longer able to

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 11/13/85	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	180.883	+ 2.045	+19.432
Loans to Depository Inst.	.791	– .334	– 3.892
Float	1.497	+ 1.128	+ .770
Total Reserve Bank Credit	198.258	+ 3.149	+18.627
Treasury Deposits with Federal Reserve Banks	3.064	– .043	– .064
Currency in Circulation	191.414	+ 1.603	+12.829
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	123.982	– 2.314	+ 6.305
	11/6/85		
Member Bank Reserves:			
Total Reserves Held	43.568	– .232	+ 5.573
Excess (Deficiency)	.788	– .017	+ .222
Net Free Reserves	.311	– .025	+ .934
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates †			
M1 (11/4/85)	611.6	+ 9.4‡	+ 11.2‡
M2 (October '85)	2,532.7	+ 6.8	+ 9.2
M3 (October '85)	3,173.6	+ 7.6	+ 8.5
Domestic Nonfinancial Debt (2nd Q'85)	6,317.3	+ 12.2	+ 13.6

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 11/15/85	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	7.36%	7.37%	7.40%
* Federal Agencies	8.00	8.45	8.95
* Municipal Notes—High Grade (46% Taxable Equivalent)	8.33	8.52	9.44
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.95	7.95	8.00

‡Finance Company Paper—Prime	
5- 14 days	8.10%
15- 29 days	8.05
30- 59 days	8.00
60- 89 days	7.90
90-179 days	7.80
180-239 days	7.80
240-270 days	7.80

‡* Bankers' Acceptances	
Dec.	7.90%
Jan.	7.95
Feb.	7.85
Mar.	7.80
Apr.	7.80
May	7.75

‡Industrial Paper—Prime	
30- 89 days	7.90%
90-120 days	7.80

†Federal Funds Effective Rate 8.75%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 3,916	$ 3,853	$ 3,695
Gross National Product (1972 Dollars)*	3rd Q'85	$ 1,685	$ 1,671	$ 1,645
Percent Change, Annual Rate	3rd Q'85	3.3	1.9	1.6
Change in Consumer Prices*	Sep '85	2.4%	2.4%	4.8%
Change in Producer Prices*	Oct '85n	10.8%	– 7.2%	– 1.2%
Civilian Employment (Thousands of Persons) †	Oct '85	107,867	107,5 4	105,649
Unemployment as % of Civilian Labor Force †	Oct '85	7.1%	7.1%	7.3%
Personal Income*	Sep '85	$ 3,209	$ 3,199	$ 3,068
Leading Indicators Composite Index (1967=100) †	Sep '85	170.3	170.2	165.7
Industrial Production Index (1977=100) †	Oct '85n	124.9	124.9r	122.7
Net Change in Consumer Installment Credit †	Sep '85n	$ 10.63	$ 6.31	$ 4.98
U.S. Merchandise Trade Balance †	Sep '85	–$ 15.55	–$ 9.90	–$ 11.54
Plant and Equipment Expenditures*	4th Q'85	$387.40(a)	$389.54(a)	$368.29
Private Housing Starts (Thousands of Units)*	Sep '85	1,583	1,746	1,669
New Construction Expenditures*	Sep '85	$ 350.4	$ 343.9	$ 321.0
Total Business Inventories †	Sep '85n	$ 579.5	$ 578.2r	$ 565.5
Total Business Sales †	Sep '85n	$ 428.5	$ 430.4r	$ 412.3

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

rely on rising prices for its natural resources to boost its standard of living. Canadians must develop a strategy to move away from emphasis on natural resource exports (which accounted for over half of their 1984 exports), toward more reliance on its manufacturing sector in order to maintain its share of global markets.

. . . But There Are Costs

While it is a fundamental principle that countries can improve their living standards by specializing in exporting what they are good at producing, this does not mean that liberalized trade carries with it no short-term costs. In both countries, there are industries which might not be able to hold their own in a more competitive market. Thus, a free-trade treaty will probably allow for an interim transitional period to give these previously protected industries time to upgrade and adapt their operations to the new free-trade environment. Adjustment assistance was built into the 1965 U.S.-Canadian auto pact, and was regarded by many to be a considerable success. Notwithstanding this, the task now facing governments in both countries is to develop a supportive structure for assisting other industries in making the necessary, albeit difficult, adjustment to a more competitive trading environment. H

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (10/30/85)	158,105	+ 704	– 1,764
New York City (11/6/85)	33,479	– 285	– 437
Commercial Paper (11/6/85)	286,403	– 362	+53,231

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (10/30/85)	252,526	+ 20	+ 3,699
New York City (11/6/85)	60,384	+ 719	– 4,053

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (10/30/85)	691,433	+ 3,723	+ 49,503
New York City (11/6/85)	153,521	+ 1,277	+ 9,651

Financial Markets

	Friday 11/15/85	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.58%	+ .12	– 1.32
180-Day Bills†	7.74	+ .10	– 1.61
Longest Bills†	7.92	+ .12	– 1.88
Recent Issues:			
$8^{7}/_{8}$s 10/31/87	8.62	+ .06	
$9^{3}/_{8}$s 9/30/89	9.18	+ .07	
$10^{1}/_{2}$s 8/15/95	9.89	+ .05	
$10^{5}/_{8}$s 8/15/15	10.74	+ .60	
Municipals:			
Bond Buyer–20 Bond Index* (11/14/85)	8.60%	– .08	– 1.71
Blue List Total ($ Million)	$1,730	$ 152	– $ 56
30-Day Visible Supply ($ Million)	$5,889	–$2,209	+ $3,322
Total	$7,619	–$2,057	+ $3,266
Corporates:			
Moody's Aa Composite (11/14/85)	11.09%	– .09	– 1.65
30-Day Visible Supply ($ Million)	$1,025	–$ 843	– $ 665
Stocks:			
Dow-Jones Averages:			
Industrials	1,435.09	+ 30.73	+ 247.15
Transportation	684.81	+ 6.67	+ 168.59
Utilities	165.83	+ 3.90	+ 22.06
65 Stocks	580.22	+ 10.78	+ 108.57
Standard and Poor's 500 Stocks	198.11	+ 4.39	+ 34.01
N.Y.S.E. Composite Index	114.35	+ 2.40	+ 19.65
N.Y.S.E. Avg. Daily Vol. for Week (000's)	132,682	+15,078	+ 59,640

* 46% Taxable equivalent 15.93%.

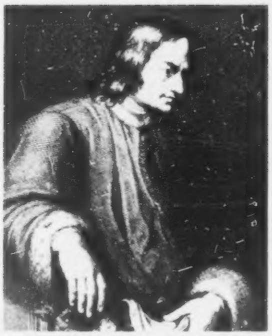
† Bond equivalent.

International Rates

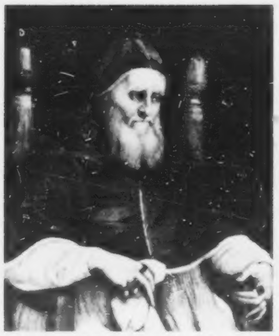
EURODOLLAR DEPOSIT RATES (bid)	Friday 11/15/85	Week Ago
Overnight	8.50%	7.81%
1 month	8.13	8.00
3 month	8.13	8.06
6 month	8.13	8.06
1 year	8.31	8.25
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.80%	9.80%
Long Term (7 to 15 yrs.)	10.35	10.35

FOREIGN EXCHANGE SPOT RATES

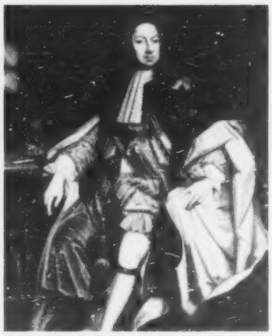
New York Opening (11/15/85)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.01893	52.8300
Canada	.7269	1.3757
Denmark	.1057	9.4600
France	.1254	7.9725
Germany	.3823	2.6155
Italy	.0005661	1766.50
Japan	.004901	204.03
Mexico	.002014	496.50
Netherlands	.3395	2.9455
Switzerland	.4661	2.1455
U.K.	1.4250	.7018



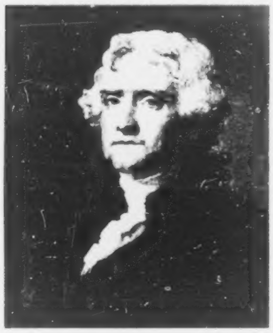
15th Century: Lorenzo de Medici and his family lead the cultural flowering of Florence.



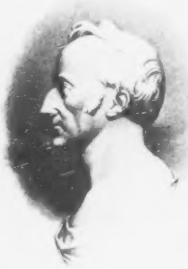
1508: Pope Julius II commissions Michelangelo to paint the Sistine ceiling.



1717: George I is honored by the composition of Handel's *Water Music*.



18th Century: Thomas Jefferson becomes a noted patron of the arts.



1829: James Smithson of London bequeaths his fortune to the U.S. to establish a museum.

1892: Andrew Carnegie provides the funds to build Carnegie Hall.

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The Manufacturers Hanover Financial Digest

Weekly Commentary, Selected Financial Data, and Business Indicators

MONDAY, NOVEMBER 25, 1985 VOLUME XXII, NUMBER 42

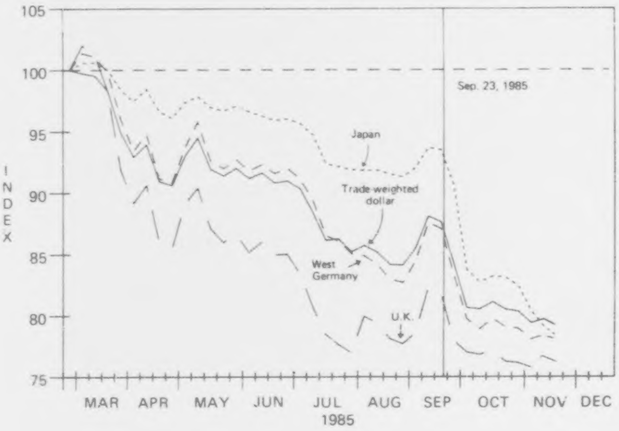
Though The Dollar Has Eased . . .

The apparent success of central bank intervention in reducing the value of the dollar against the world's other major trading currencies has demonstrated the power of coordinated action by the major central banks. Since the finance ministers and central bank governors of the "G-5" group of industrial countries—the United States, West Germany, Japan, France and the United Kingdom—met in New York last September 22, the dollar has depreciated significantly against all of their currencies (see chart). But even before that gathering there had been growing interest in modifying the existing international monetary system. As a result an international monetary conference was held in Washington, D.C. in early November sponsored by two members of Congress, Senator Bill Bradley (D-NJ) and Representative Jack Kemp (R-NY), to discuss reform of the existing floating exchange rate system—an idea whose time may have come.

Actually the recent decline of the dollar is part of a longer-term trend which began in late February when the external value of the dollar peaked. Since that time, the dollar has depreciated on a trade-weighted basis by about 21 percent, of which over nine percentage points has occurred since September 22. The G-5 meeting did, however, accelerate the dollar's fall, particularly against the Japanese yen. The decision by the conferees to undertake a coordinated program to reduce the dollar's external value represents a major step toward international economic cooperation. The effectiveness of this decision was, however, greatly facilitated by the fact that it coincided with the ongoing trend of the foreign exchange markets, rather than an attempt to turn the market around as were most of the previous (and unsuccessful) intervention schemes.

What is more, the G-5 agreement commits the U.S. to a more active role in the exchange markets. This reverses, or at least modifies the prior U.S. policy of intervention only when there was the threat of a "disorderly market"—a term never clearly defined. Although the level and timing of intervention by all of the five central banks is not entirely clear, it is estimated that the total amount of dollars sold by the central banks since September 22 has been over $8 billion. Whereas this amount would have been a mere drop in the bucket in the face of a strong demand for dollars, it has obviously been sufficient at the margin to reinforce the market's recent direction. The chart clearly illustrates the acceleration of the trend immediately following the September meeting.

U.S. DOLLAR DEPRECIATION VS. SELECTED CURRENCIES
(FEBRUARY 27, 1985 = 100)



. . . Longer-Term Measures Are Needed . . .

Although the downward course of the dollar speeded up sharply in the two weeks after the G-5 meeting, since that time, with the exception of Japan, the effect has attenuated with the U.S. currency reverting more toward the longer-term trend. The sharp appreciation of the yen against the dollar has continued, however, due to a sustained and well-publicized policy of strong intervention by Japan and the introduction of domestic policies designed to support it.

Since the end of last September, interest rates have risen substantially in Japan. For example, the three-month Euroyen rate rose from 6.3 percent on September 20 to 7.7 percent on November 15. In the same period, the equivalent U.S. rate fell by three-tenths of a percent. The other G-5 countries have not yet taken clear-cut steps to modify their domestic policies, and it shows in their exchange

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rates against the dollar. The three-month Euromark rate, for example, has only risen by 0.3 percent and the Eurosterling rate by 0.2 percent, compared with the Euroyen's increase of 1.4 percent. Indeed, the Japanese currency last week approached the 200 yen to the dollar level which has been widely suggested as the dollar/yen exchange rate level to which the Bank of Japan aspires.

It is clear that intervention alone will not be adequate to force the dollar down to levels desired by the G-5 members or to keep it down on a sustained basis. As the G-5 joint members' statement points out, there is a need for both a convergence of domestic economic policies and readiness to cooperate more closely, particularly in the areas of monetary and fiscal policies. To date, this coordination and cooperation has been sporadic at best.

In fact, prospects for stronger growth next year in the United States than in most of the other industrial nations, combined with the probability of continuing large U.S. budget, trade and current account deficits, and consequently, higher real interest rates, might well boost the demand for dollars. If so, an accommodative, and probably inflationary, monetary policy in this country would be needed to keep the dollar from rising again in the foreign exchange markets. If the Fed should tighten monetary policy, the dollar could again bounce up.

Between July, 1980 when it began its rapid appreciation and February, 1985 when it peaked, the dollar appreciated by 92 percent on a trade-

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 11/20/85	$ Change Since	
		Week Ago	Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	179.798	– 1.085	+15.665
Loans to Depository Inst.	1.565	+ .774	– 2.703
Float	1.556	+ .059	+ .664
Total Reserve Bank Credit	196.580	– 1.678	+16.334
Treasury Deposits with Federal Reserve Banks	3.008	– .056	– .501
Currency in Circulation	191.568	+ .177	+12.467
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	124.617	+ .635	+ 6.940
	11/20/85		
Member Bank Reserves:			
Total Reserves Held	44.717	+ 1.115	+ 5.862
Excess (Deficiency)	.980	+ .157	+ .385
Net Free Reserves	.324	– .022	+ .316

Monetary Aggregates †		% Change Since	
		Three Months Ago*	Year Ago
M1 (11/11/85)	613.6	+ 9.0‡	+ 11.4‡
M2 (October '85)	2,533.4	+ 6.9	+ 9.2
M3 (October '85)	3,174.5	+ 7.7	+ 8.5
Domestic Nonfinancial Debt (2nd Q'85)	6,317.3	+ 12.2	+ 13.6

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 11/22/85	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	7.23%	7.30%	7.31%
* Federal Agencies	7.47	7.49	7.52
* Municipal Notes—High Grade (46% Taxable Equivalent)	8.60	9.26	9.44
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.75	7.75	7.85

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	7.60%	Dec.	7.75%
15- 29 days	7.70	Jan.	7.70
30- 59 days	7.75	Feb.	7.70
60- 89 days	7.75	Mar.	7.65
90-179 days	7.66	Apr.	7.60
180-239 days	7.50	May	7.55
240-270 days	7.50		

‡ Industrial Paper—Prime			
30- 89 days	7.75%	†Federal Funds Effective Rate	7.40%
90-120 days	7.70		

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 3,916 r	$ 3,853	$ 3,695
Gross National Product (1972 Dollars)*	3rd Q'85	$ 1,689 r	$ 1,671	$ 1,645
Percent Change, Annual Rate	3rd Q'85	4.3 r	1.9	1.6
Change in Consumer Prices*	Oct '85n	3.6%	2.4%	3.6%
Change in Producer Prices*	Oct '85	10.8%	– 7.2%	– 1.2%
Civilian Employment (Thousands of Persons) †	Oct '85	107,867	107,544	105,649
Unemployment as % of Civilian Labor Force †	Oct '85	7.1%	7.1%	7.3%
Personal Income*	Oct '85n	$ 3,221	$ 3,207 r	$ 3,079
Leading Indicators Composite Index (1967=100) †	Sep '85	170.3	170.2	165.7
Industrial Production Index (1977=100) †	Oct '85	124.9	124.9	122.7
Net Change in Consumer Installment Credit †	Sep '85	$ 10.63	$ 6.31	$ 4.98
U.S. Merchandise Trade Balance †	Sep '85	–$ 15.55	–$ 9.90	–$ 11.54
Plant and Equipment Expenditures*	4th Q'85	$387.40(a)	$389.54(a)	$368.29
Private Housing Starts (Thousands of Units)*	Oct '85n	1,760	1,589 r	1,564
New Construction Expenditures*	Sep '85	$ 350.4	$ 343.9	$ 321.0
Total Business Inventories †	Sep '85	$ 579.5	$ 578.2	$ 565.5
Total Business Sales †	Sep '85	$ 428.5	$ 430.4	$ 412.3

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

weighted basis only to plunge by about 21 percent since then. The often rapid and extreme fluctuations of the U.S. currency against those of our trading partners have been a major factor in the current global economic malaise, distorting trade flows, agitating financial markets and creating wide disparities in balance of payments performance.

. . . Including Monetary Reform

The November international monetary conference meeting in Washington explored a wide range of possible alternative methods to reduce foreign exchange market volatility. On one side are those who contend that the present floating system with all of its many defects is, nonetheless, better than the alternatives. At the other end of the spectrum are the advocates of more rigid systems such as a return to a system of fixed exchange rate relationships between currencies, or one based upon an abstract standard such as gold against which each currency has a fixed value.

Whatever kind of system may eventually evolve, it is clear that its efficacy will depend on a recognition that the enormous growth in integration and interdependence of the global economy since the end of World War II demands increasing coordination of national economic policies as a fundamental prerequisite for exchange rate stability. Just as widely varied rates of inflation finally broke the fixed-rate Bretton Woods system in the early 1970s, so, too, the wide discrepancies in trade performance and international financial flows threaten the present floating rate regime.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (11/6/85)	157,269	– 962	– 2,049
New York City (11/13/85)	33,114	– 365	– 743
Commercial Paper (11/13/85)	288,343	+ 1,966	+54,248

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (11/6/85)	255,001	+ 2,425	+ 4,184
New York City (11/13/85)	59,700	– 684	– 4,590

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (11/6/85)	696,570	+ 4,955	+ 50,941
New York City (11/13/85)	152,752	– 570	+ 8,704

Financial Markets

	Friday 11/22/85	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.46%	– .12	– 1.34
180-Day Bills†	7.68	– .06	– 1.47
Longest Bills†	7.81	– .11	– 1.74
Recent Issues:			
$8\frac{1}{2}$s 11/30/87 (When Issued)	8.53	NA	
$9\frac{3}{8}$s 9/30/89	9.01	– .17	
$9\frac{1}{2}$s 11/15/95 (When Issued)	9.62	NA	
$10\frac{5}{8}$s 8/15/15	9.96	– .78	
Municipals:			
Bond Buyer–20 Bond Index* (11/21/85)	8.37%	– .23	– 1.94
Blue List Total ($ Million)	$1,628	–$ 102	– $ 174
30-Day Visible Supply ($ Million)	$4,886	–$1,003	+ $2,568
Total	$6,514	–$1,105	+ $2,394
Corporates:			
Moody's Aa Composite (11/21/85)	10.94%	– .15	– 1.70
30-Day Visible Supply ($ Million)	$1,798	+$ 773	– $2,002
Stocks:			
Dow-Jones Averages:			
Industrials	1,460.78	+ 25.69	+ 259.26
Transportation	687.50	+ 2.69	+ 163.92
Utilities	165.88	+ .05	+ 22.21
65 Stocks	586.88	+ 6.66	+ 110.40
Standard and Poor's 500 Stocks	201.52	+ 3.41	+ 37.00
N.Y.S.E. Composite Index	116.24	+ 1.89	+ 21.45
N.Y.S.E. Avg. Daily Vol. for Week (000's)	124,996	– 7,686	+ 46,626

* 46% Taxable equivalent 15.50%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 11/22/85	Week Ago
Overnight	7.56%	8.50%
1 month	8.00	8.13
3 month	8.00	8.13
6 month	8.00	8.13
1 year	8.19	8.31
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.50%	9.80%
Long Term (7 to 15 yrs.)	10.05	10.35

FOREIGN EXCHANGE SPOT RATES

New York Opening (11/22/85)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.01913	52.2800
Canada	.7270	1.3755
Denmark	.1071	9.3350
France	.1269	7.8775
Germany	.3869	2.5845
Italy	.0005732	1744.50
Japan	.004958	201.70
Mexico	.002014	496.50
Netherlands	.3436	2.9103
Switzerland	.4725	2.1165
U.K.	1.4460	.6916

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The Manufacturers
Hanover
Financial
Digest
Weekly Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, DECEMBER 2, 1985
VOLUME XXII, NUMBER 43

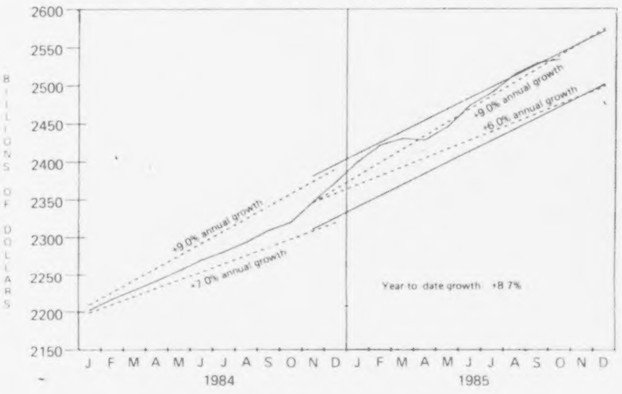
Monetary Policy May Remain On Hold . . .

Amid a continuing barrage of mixed economic signals, still modest rates of inflation, within-target M2 and M3 money supply growth and, perhaps most important, widespread expectations that an easing of monetary policy is just around the corner, powerful bond and stock market rallies erupted in recent weeks—sending bond yields tumbling and share prices soaring. However, despite the current bullish sentiment, the financial markets may have gotten ahead of themselves. The combination of an upward revision of third-quarter GNP and rapid M1 money supply growth could cause the Federal Reserve to hesitate before easing monetary policy further. Add to this the need to guide the dollar lower gradually, rather than all at once, and the likelihood of a steady, yet quite accommodative monetary policy posture in the weeks ahead becomes an even better bet. While this could change quickly if the pace of business softens, it may be early January before such evidence would become available.

In the economy itself, the appearance of economic sluggishness has been viewed as good news by the debt markets. It raises the possibility of greater monetary policy ease in order to stimulate the economy—and, as a result, lower interest rates and higher bond prices. Nor does one have to look far to find signs of economic malaise, especially in the manufacturing sector. Factory orders remain weak, industrial production is only slightly higher than a year ago and capacity utilization rates nationwide are actually lower. What is more, auto sales have tumbled since the elimination of dealer financing incentives, and building permits have headed south as well. So far, so good—at least for the debt markets. However, despite all this, third quarter real gross national product growth was revised upward from a 3.3 percent to a 4.3 percent annual clip, while the rise in inflation-adjusted domestic demand—which nets out of GNP the growth retarding effects of the trade deficit—was even more brisk, advancing at a nearly 5½ percent seasonally adjusted annual rate. Not bad, for an economy supposedly moving sideways at best.

But that's yesterday's news. Perhaps more important is the fact that GNP growth in the current quarter could be relatively brisk as well—despite the easing of auto sales and signs of a slowing in consumer spending in general. For one thing, although auto sales are now running some 33 percent below the torrid, third quarter pace, automakers continue to schedule, and stick to, hefty production schedules. While this cannot continue forever, that's not what counts for now. For rather than subtracting from GNP growth, the growing divergence between sales and production could actually increase it, with today's involuntary buildup in auto stocks showing up in the fourth quarter gross national product as a sizable increase in inventory accumulation. For another, any improvement in the trade balance deficit in the current quarter will also be a plus, further boosting GNP growth. On balance, while recent business trends do not preclude another round of Fed easing, they may not hasten it either.

MONEY SUPPLY, M2



. . . Despite Widespread Expectations . . .

Much the same can be said of recent money supply developments. Take, for example, the M1 money numbers. Despite repeated disclaimers, there is still a lingering suspicion that M1 matters—at least to some extent. If it does, the news is not good. After slowing in October, the growth of this measure has actually perked up again, advancing at a nearly five percent annual rate over the last four weeks, compared with almost no growth during the immediately preceding four weeks. What is more, this money supply measure now stands some $8 billion

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above its rebased 1985 upper target boundary. However, on the other hand, the year-to-date growth of the closely watched M2 money number is now within its narrow target boundaries for the first time since last spring (see chart), while M3 remains squarely within its target ranges. The Fed thus finds itself with two of its three money supply numbers under control—a further justification for ignoring M1, if desired. But, as with recent business trends, money supply developments, too, can be used as a rationale for whatever the Fed wants to do, whether maintaining policy on hold, or switching toward greater ease.

So, too, the dollar's influence on Fed policy cannot be minimized. Despite all the talk of a weak dollar, it remains some 50 percent higher on a trade-weighted basis than where it stood in mid-1980 (Financial Digest—November 25, 1985). What is more, the dollar's persistent strength is again affecting adversely the outlook for global economic activity. One example is the recent rise in Japanese interest rates in order to strengthen the yen—a move clearly at cross-purposes with official efforts to stimulate Japanese economic growth. While it has resulted in a further appreciation of the yen against the dollar, a longer-lasting solution to the problem of U.S. manufacturers in general, and exporters in particular, remains faster, not slower economic growth in the other industrial countries.

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 11/20/85	$ Change Since	
		Week Ago	Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	179.798	– 1.085	+15.665
Loans to Depository Inst.	1.565	+ .774	– 2.703
Float	1.556	+ .059	+ .664
Total Reserve Bank Credit	196.580	– 1.678	+16.334
Treasury Deposits with Federal Reserve Banks	3.008	– .056	– .501
Currency in Circulation	191.568	+ .177	+12.467
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	124.617	+ .635	+ 6.940
	11/20/85		
Member Bank Reserves:			
Total Reserves Held	44.717	+ 1.115	+ 5.862
Excess (Deficiency)	.980	+ .157	+ .385
Net Free Reserves	.324	– .022	+ .316

		% Change Since	
Monetary Aggregates †		Three Months Ago*	Year Ago
M1 (11/18/85)	616.6	+ 8.0‡	+ 11.7‡
M2 (October '85)	2,533.4	+ 6.9	+ 9.2
M3 (October '85)	3,174.5	+ 7.7	+ 8.5
Domestic Nonfinancial Debt (2nd Q'85)	6,317.3	+ 12.2	+ 13.6

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 11/29/85	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	7.15%	7.25%	7.30%
* Federal Agencies	7.40	7.45	7.50
* Municipal Notes—High Grade (46% Taxable Equivalent)	9.26	10.19	10.65
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.85	7.85	7.90

‡ Finance Company Paper—Prime	
5- 14 days	7.70%
15- 29 days	7.80
30- 59 days	7.80
60- 89 days	7.80
90-179 days	7.77
180-239 days	7.75
240-270 days	7.75

‡* Bankers' Acceptances	
Dec.	7.80%
Jan.	7.75
Feb.	7.70
Mar.	7.65
Apr.	7.65
May	7.60

‡ Industrial Paper—Prime	
30- 89 days	7.80%
90-120 days	7.80

† Federal Funds Effective Rate 9.00%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

		Latest Period or End of Period	Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 3,916	$ 3,853	$ 3,695
Gross National Product (1972 Dollars)*	3rd Q'85	$ 1,689	$ 1,671	$ 1,645
Percent Change, Annual Rate	3rd Q'85	4.3	1.9	1.6
Change in Consumer Prices*	Oct '85	3.6%	2.4%	3.6%
Change in Producer Prices*	Oct '85	10.8%	– 7.2%	– 1.2%
Civilian Employment (Thousands of Persons) †	Oct '85	107,867	107,544	105,649
Unemployment as % of Civilian Labor Force †	Oct '85	7.1%	7.1%	7.3%
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Industrial Production Index (1977=100) †	Oct '85	124.9	124.9	122.7
Net Change in Consumer Installment Credit †	Sep '85	$ 10.63	$ 6.31	$ 4.98
U.S. Merchandise Trade Balance †	Oct '85n	–$ 11.45	–$ 15.55	–$ 9.65
Plant and Equipment Expenditures*	4th Q'85	$387.40(a)	$389.54(a)	$368.29
Private Housing Starts (Thousands of Units)*	Oct '85	1,760	1,589	1,564
New Construction Expenditures*	Sep '85	$ 350.4	$ 343.9	$ 321.0
Total Business Inventories †	Sep '85	$ 579.5	$ 578.2	$ 565.5
Total Business Sales †	Sep '85	$ 428.5	$ 430.4	$ 412.3

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

. . . Of An Imminent Turn Toward Ease

Although the desire to lower the dollar's external value tends to suggest the need for more accommodation and lower interest rates here, the most obvious course of action may not be the most appropriate. Getting the dollar lower in the foreign exchange markets is one thing; a rapidly depreciating currency and a revival of inflation expectations is another. As with recent business trends and money supply developments, the Fed has to walk a fine, and sometimes conflicting line—balancing the obvious benefits of more ease, against some less apparent problems which could arise from such a move.

What's the bottom line? For one thing, in light of the ongoing liquidity problems of some advanced developing countries as well as the virtual absence of any significant inflation rate pressures, it is unlikely that the Federal Reserve would tighten the money and credit reins. On the other hand, it may hesitate before easing further, given the better GNP numbers, rapid M1 growth, and a desire not to touch off too quick a depreciation of the dollar in the foreign exchange markets. Only if the pace of business clearly softens, and the Christmas selling season falters would the stage be set for another round of ease. This may, however, have to await the turn of the year, when December's business numbers begin to filter in.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since	
		Week Ago	Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (11/13/85)	157,069	– 238	– 1,738
New York City (11/13/85)	33,114	– 365	– 743
Commercial Paper (11/13/85)	288,343	+ 1,966	+54,248

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since	
		Week Ago	Year Ago
Nationwide (11/13/85)	253,526	– 1,488	+ 3,268
New York City (11/13/85)	59,700	– 684	– 4,590

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since	
		Week Ago	Year Ago
Nationwide (11/13/85)	697,939	– 949	+ 51,801
New York City (11/13/85)	152,752	– 570	+ 8,704

Financial Markets

	Friday 11/29/85	Change Since	
		Week Ago	Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.39%	– .07	– 1.36
180-Day Bills†	7.64	– .04	– 1.51
Longest Bills†	7.84	+ .03	– 1.86
Recent Issues:			
8 1/2s 11/30/87	8.49	– .04	
9 3/8s 9/30/89	8.95	– .06	
9 1/2s 11/15/95	9.59	– .03	
9 7/8s 11/15/15 (When Issued)	9.86	NA	
Municipals:			
Bond Buyer–20 Bond Index* (11/27/85)	8.51%	+ .14	– 1.53
Blue List Total ($ Million)	$2,033	+$ 405	+ $ 383
30-Day Visible Supply ($ Million)	$7,712	+$2,826	+ $4,709
Total	$9,745	+$3,231	+ $5,092
Corporates:			
Moody's Aa Composite (11/26/85)	10.97%	– .01	– 1.53
30-Day Visible Supply ($ Million)	$2,158	+$ 360	+ $ 658
Stocks:			
Dow-Jones Averages:			
Industrials	1,472.13	+ 11.35	+ 283.19
Transportation	690.31	+ 2.81	+ 168.06
Utilities	164.03	– 1.85	+ 18.41
65 Stocks	589.22	+ 2.34	+ 115.02
Standard and Poor's 500 Stocks	202.17	+ .65	+ 38.59
N.Y.S.E. Composite Index	116.55	+ .31	+ 22.25
N.Y.S.E. Avg. Daily Vol. for Week (000's)	110,848	–14,148	+ 28,334

* 46% Taxable equivalent 15.76%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 11/29/85	Week Ago
Overnight	7.88%	7.56%
1 month	8.06	8.00
3 month	8.06	8.00
6 month	8.06	8.00
1 year	8.19	8.19
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.46%	9.50%
Long Term (7 to 15 yrs.)	10.03	10.05

FOREIGN EXCHANGE SPOT RATES

New York Opening (11/29/85)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.01963	50.9500
Canada	.7253	1.3788
Denmark	.1090	9.1725
France	.1305	7.6650
Germany	.3979	2.5130
Italy	.0005867	1704.50
Japan	.004949	202.08
Mexico	.002051	487.50
Netherlands	.3539	2.8258
Switzerland	.4805	2.0810
U.K.	1.4830	.6743

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The Manufacturers Hanover Financial Digest

Weekly Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, DECEMBER 9, 1985 VOLUME XXII, NUMBER 44

Falling Commodity Prices . . .

Sometimes lost in the discussions of international trade issues is the extended decline in prices for those basic commodities which form the principal exports of the developing countries. After peaking in 1980 commodity prices plunged, reaching their recent lows in 1982 (see chart). Global commodity prices (as reflected in the International Monetary Fund's Commodity Price Index) began to recover with the rapid expansion of U.S. economic activity which began in November of that year. In the third quarter of 1984, however, as real U.S. growth eased without a compensating increase in economic activity elsewhere, global commodity prices again began to fall.

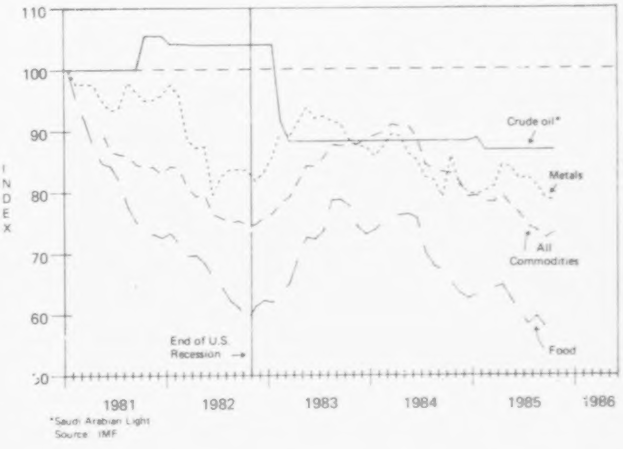
Adding to the economic impact of the decline in demand occasioned by the slowing of economic activity has been the continuation of high debt service costs and a weakening of the trade-weighted dollar. The latter has reduced the purchasing power of those countries whose export earnings are principally in dollars. This has made suppliers, some of whom were encouraged to enter the market or increase production by the skyrocketing prices in the decade of the 1970s, maintain and, where possible, increase production in spite of falling prices. The results have been an even greater excess of supply over demand, reinforcing the decline in most commodities' prices.

The price decline has been consistent through the major commodity categories. Food prices, for example, reflecting excellent harvests in recent years fell by 13.7 percent between the third quarter of 1984 and the third quarter of 1985 and are six percent below their low point in 1982. And prices of beverages (coffee, tea, cocoa) and agricultural raw materials averaged 19 percent and 14 percent respectively below year earlier levels.

. . . Reflect Excess Supply . . .

Oil prices, too, reflect the current malaise in commodity prices. In spite of the strenuous efforts of OPEC, oil prices now respond to market forces. One major reason for this has been the entry into the market of some substantial oil-producing countries which have opted not to join OPEC, thus undermining the cartel's efforts to control world supplies. Even the Saudi Arabians, the key oil producers, have recently abandoned efforts to hold the price line through production cutbacks and instead have chosen to increase output. Further, they have developed bilateral agreements with favored clients at negotiated prices. These deals have undercut the open markets and, as a result have put downward pressure on other crude producers and refiners.

SELECTED COMMODITY PRICE INDEXES
(JANUARY 1981 = 100)



*Saudi Arabian Light
Source: IMF

Through the end of November, spot prices for all OPEC crudes averaged $26.60 per barrel—3½ percent below their levels for the same period in 1984. Saudi Arabian light, the so-called benchmark crude, has averaged $27.50 per barrel this year, two percent below last year's level. Once winter demand fades, spot crude prices may fall even further.

Of all the major categories, metal prices have been the most depressed. In fact, metal prices have benefited less from the current economic upswing than most other commodity categories; last year metal prices fell back below their 1982 low point. The weakness in metals prices owes much to changes in technology in recent years as well as an overall secular decline in heavy construction and machine building. Plastics and other materials have replaced metals in many instances. In spite of strenuous

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efforts by groups of metal producers to sustain stable prices through holding huge buffer stocks, declining demand for metal reflecting both a slowing of cyclical economic activity and technological change has forced prices down.

Illustrative of these problems is the crisis in the tin industry. The International Tin Council (ITC) has been unable to meet its contractional obligations, resulting in a suspension of tin trading on the London Metal Exchange on October 24. This event called into question the reliability of the present system of international metal commodities trade and, besides tin, is affecting copper, zinc, aluminum, lead and nickel. In the presence of large inventories of most of these metals, uncertainty as to the financial viability of existing sales and futures contracts has recently forced world prices markedly lower. Indeed, in the case of tin there may be as much as 340 thousand metric tons in world inventories against an annual average demand of perhaps 190 thousand metric tons—nearly two years' supply.

. . . And Sluggish Demand

Several other metals show a similar excess of supply over demand. What is more, the problems of the metal producers are being echoed in other cartels which aim at sustaining commodity prices through agreements to buy up excess production. In an era of high interest rates, such inventories become prohibitively expensive—as the problems of the ITC show. If the tin cartel falls, others may disappear as well, leading to freer trade in commodities in

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 12/4/85	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	182.449	+ 2.838	+17.510
Loans to Depository Inst.	1.573	− 2.709	− 2.780
Float	1.214	− .044	+ .701
Total Reserve Bank Credit	199.319	+ .472	+18.397
Treasury Deposits with Federal Reserve Banks	2.258	− .329	− .328
Currency in Circulation	193.745	+ 1.995	+14.016
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	127.174	+ .623	+ 6.738
	12/4/85		
Member Bank Reserves:			
Total Reserves Held	45.244	+ .634	+ 6.280
Excess (Deficiency)	1.084	+ .190	+ .170
Net Borrowed Reserves	1.341	+ 1.579	+ 1.493
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates †			
M1 (11/25/85)	621.0	+ 7.3‡	+ 11.2‡
M2 (October '85)	2,533.3	+ 6.9	+ 9.2
M3 (October '85)	3,177.2	+ 7.9	+ 8.6
Domestic Nonfinancial Debt (2nd Q'85)	6,317.3	+ 12.2	+ 13.6

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 12/6/85	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	7.26%	7.32%	7.36%
* Federal Agencies	7.50	7.52	7.54
* Municipal Notes—High Grade (46% Taxable Equivalent)	10.00	10.37	10.93
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.97	8.00	7.65

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	7.88%	Jan.	7.90%
15- 29 days	7.89	Feb.	7.85
30- 59 days	7.90	Mar.	7.80
60- 89 days	7.90	Apr.	7.75
90-179 days	7.82	May	7.70
180-239 days	7.70	Jun.	7.68
240-270 days	7.70		

‡Industrial Paper—Prime			
30- 89 days	7.80%	†Federal Funds	
90-120 days	7.75	Effective Rate	7.94%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 3,916	$ 3,853	$ 3,695
Gross National Product (1972 Dollars)*	3rd Q'85	$ 1,689	$ 1,671	$ 1,645
Percent Change, Annual Rate	3rd Q'85	4.3	1.9	1.6
Change in Consumer Prices*	Oct '85	3.6%	2.4%	3.6%
Change in Producer Prices*	Oct '85	10.8%	− 7.2%	− 1.2%
Civilian Employment (Thousands of Persons) †	Nov '85n	107,927	107,867	105,932
Unemployment as % of Civilian Labor Force †	Nov '85n	7.0%	7.1%	7.1%
Personal Income*	Oct '85	$ 3,221	$ 3,207	$ 3,079
Leading Indicators Composite Index (1967=100) †	Oct '85n	171.1	170.6r	164.2
Industrial Production Index (1977=100) †	Oct '85	124.9	124.9	122.7
Net Change in Consumer Installment Credit †	Sep '85	$ 10.63	$ 6.31	$ 4.98
U.S. Merchandise Trade Balance †	Oct '85	−$ 11.45	−$ 15.55	−$ 9.65
Plant and Equipment Expenditures*	4th Q'85	$387.40(a)	$389.54(a)	$368.29
Private Housing Starts (Thousands of Units)*	Oct '85	1,760	1,589	1,564
New Construction Expenditures*	Oct '85n	$ 347.8	$ 346.1r	$ 318.2
Total Business Inventories †	Sep '85	$ 579.5	$ 578.2	$ 565.5
Total Business Sales †	Sep '85	$ 428.5	$ 430.4	$ 412.3

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

general. In fact, the age of commodity cartels, which afforded high and stable prices to the developing countries in the postwar period, may have ended due to the high costs of holding stockpiles in the lower growth era of the 1980s.

The implications of falling commodity prices for the global economy—industrial and developing countries alike—are important. Clearly a fall in the price of basic commodities is deflationary. Lower cost inputs will lead to lower prices, benefiting consumers. Since transactions for many of these commodities are conducted in dollars, the recent decline in the value of the dollar will drive prices down even further in terms of many foreign currencies. This will stimulate economic growth, particularly in the other industrial countries, and improve their competitive position. Thus, while the U.S. will benefit to some degree from declining commodity prices, our trading partners may well benefit more.

The developing countries, many of which are highly dependent upon exports of a single (or a few) basic commodities, may see their foreign exchange earnings suffer further erosion as the dollar eases and demand for commodities remain sluggish. This will impose additional burdens on them. They are already being severely tested by their present debt service obligations, and the need to pay for imports. What is more, the new orientation toward growth rather than austerity for the high-debt developing countries will, at least at first, call for higher debt service costs, imposing even greater burdens on export earnings.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (11/20/85)	156,908	– 114	– 2,707
New York City (11/27/85)	33,458	– 310	– 490
Commercial Paper (11/27/85)	290,805	– 8	+52,697

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (11/20/85)	254,340	+ 814	+ 3,901
New York City (11/27/85)	59,236	– 169	– 4,220

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (11/20/85)	706,680	+ 8,854	+ 60,229
New York City (11/27/85)	157,192	– 2,364	+ 14,488

Financial Markets

	Friday 12/6/85	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.48%	+ .09	– 1.22
180-Day Bills†	7.69	+ .05	– 1.41
Longest Bills†	7.88	+ .04	– 1.72
Recent Issues:			
$8^{1}/_{2}$s 11/30/87	8.46	– .03	
$9^{3}/_{8}$s 9/30/89	9.00	+ .05	
$9^{1}/_{2}$s 11/15/95	9.63	+ .04	
$9^{7}/_{8}$s 11/15/15	9.89	+ .03	
Municipals:			
Bond Buyer–20 Bond Index* (12/5/85)	8.54%	+ .03	– 1.41
Blue List Total ($ Million)	$2,338	+$ 305	+ $ 453
30-Day Visible Supply ($ Million)	$5,360	–$2,352	+ $3,648
Total	$7,698	–$2,047	+ $4,101
Corporates:			
Moody's Aa Composite (12/5/85)	10.92%	– .05	– 1.63
30-Day Visible Supply ($ Million)	$1,580	–$ 578	+ $ 100
Stocks:			
Dow-Jones Averages:			
Industrials	1,477.18	+ 5.05	+ 313.97
Transportation	693.59	+ 3.28	+ 170.89
Utilities	165.57	+ 1.54	+ 20.92
65 Stocks	591.96	+ 2.74	+ 124.18
Standard and Poor's 500 Stocks	202.99	+ .82	+ 40.73
N.Y.S.E. Composite Index	116.99	+ .44	+ 23.47
N.Y.S.E. Avg. Daily Vol. for Week (000's)	135,032	+24,184	+ 46,256

* 46% Taxable equivalent 15.81%.

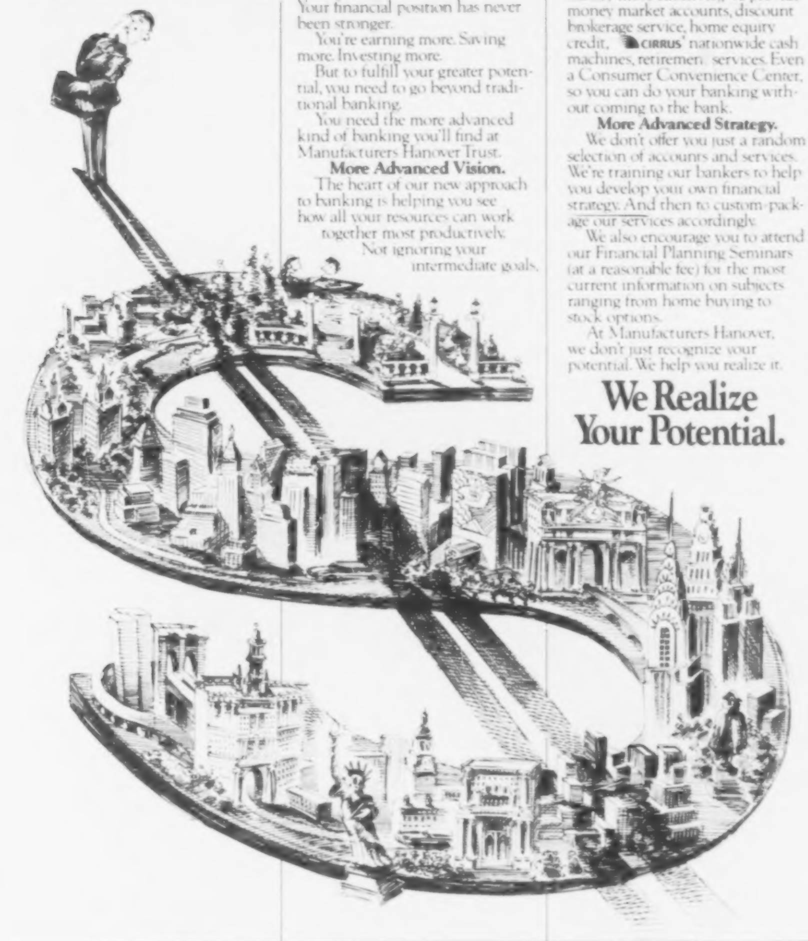
† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 12/6/85	Week Ago
Overnight	8.00%	7.88%
1 month	8.19	8.06
3 month	8.13	8.06
6 month	8.13	8.06
1 year	8.31	8.19
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.50%	9.46%
Long Term (7 to 15 yrs.)	10.00	10.03

FOREIGN EXCHANGE SPOT RATES

New York Opening (12/6/85)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.01948	51.3400
Canada	.7165	1.3956
Denmark	.1094	9.1425
France	.1299	7.7000
Germany	.3962	2.5240
Italy	.0005806	1722.50
Japan	.004917	203.38
Mexico	.002107	474.50
Netherlands	.3521	2.8405
Switzerland	.4753	2.1040
U.K.	1.4765	.6773



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The Manufacturers Hanover Financial Digest

Weekly Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, DECEMBER 16, 1985
VOLUME XXII, NUMBER 45

OPEC Has A New Deal . . .

It is a little ironic that as members of the Organization of Petroleum Exporting Countries (OPEC) were alerting world markets to the likelihood of lower oil prices at their meeting in Geneva last week, spot prices for their crudes had been rallying from their summer lows. In the last two months, a few premium grades actually posted their highest prices this year. Yet OPEC is not merely posturing; it is coming to grips with some of the fundamental challenges and changes in oil markets. After four years of trying and failing to maintain prices by reducing supplies—at first by exhorting members to restrain output and then by setting output quotas—OPEC has officially abandoned these price-supporting tactics. The cartel is attempting to recover some of its losses in market share—thereby reestablishing its control over prices—by raising crude oil production and by negotiating prices for this oil on a "netback" basis. This method allows prices for crude to be determined by market conditions.

In recent years OPEC has lost its preeminence in world oil markets to outside producers. Its share of world supplies dropped from 49 percent in 1981, to just over one-third today. Increased output from the North Sea producers, Mexico, the Soviet Union, Australia and China has offset OPEC's cutbacks. At the same time, total world demand for crude oil dropped sharply in response to the second round of price hikes beginning in 1979. Oil consumption in the countries belonging to the Organization for Economic Cooperation and Development (OECD) has fallen 17 percent from an average of 41 million barrels a day in 1979, to an estimated 34 million barrels a day this year.

. . . But Consumers Are Not Buying

After abandoning attempts to support prices by restricting output, OPEC, in October, raised output to an average of 17.3 million barrels a day. This is up from the now defunct 16 million barrels a day quota and well above the average of 15.4 million barrels a day registered in the first half of 1985. That prices have not slipped further is attributable to seasonal demand, a limited rebuilding of inventories and the weakness of the U.S. dollar. Indeed the latter factor has allowed an average 12 percent decline in local currency costs paid by European and Japanese importers since September.

While it may appear that the conjunction of lower prices and a weakening U.S. dollar—the standard denomination of most oil sales—would trigger stronger demand, with the few exceptions of Japan, West Germany and the United States, most oil importing countries lack the vigor and stimulative government policies such a development normally requires. For the developing economies in Latin America and Africa, depressed prices for their exports of primary commodities and restrictive external debt conditions will curb any inclination to step up oil imports. World demand for crude oil may not pick up substantially until prices fall further.

For The Nation's Retailers . . .

Prospects for lower oil prices represent an unexpected Christmas gift to American consumers. Although lower prices may not materialize until after the Christmas shopping season is over, anticipation of these savings may lift consumers' spirits and enthusiasm to spend. Even now, just about every major retailer across the country reports that the Holiday selling season has gotten off to a strong start. Further, the Commerce Department's preliminary estimate of November's retail sales seems to confirm that the nation's cash registers indeed are ringing up a merry tune. Boosted by heavy buying during the Thanksgiving weekend, retail sales, excluding automobile purchases, rose a seasonally adjusted 1.2 percent compared with October—the largest rise in eight months.

Retailers are rejoicing over the early turnout. For many merchants, Christmas sales can add up to almost half of their annual volume and account for two-thirds of their profits. Strong sales are particularly important today to provide a good launching pad for 1986 and to keep the economy out of recession. One possible constraint might be the fact that the season is shorter. Because Thanksgiving, which marks the beginning of the traditional Holiday shopping season, was extremely late this

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year, there are only 26 days between Thanksgiving and Christmas compared with 32 days last year. Therefore, merchants need higher sales each day just to match last year's seasonal performance. On the other hand, retailers may find a silver lining in the shorter Holiday selling period since consumers now have less time for extensive browsing and bargain hunting to take care of their shopping lists.

. . . It's A Season To Be Jolly

Retailers should be encouraged by the results of a recent survey conducted by the Conference Board. It showed that households plan to spend, on average, $315 on Christmas presents this year, about five percent more than in 1984. With nearly 87 million households nationwide, this translates into more than $27 billion of spending on gifts alone.

Inventories are another bright spot for retailers. Last year, merchants stocked up heavily in anticipation of strong Holiday buying. Sales, however, fell short of expectations and retailers had to resort to substantial markdowns early in the Holiday season to clear out surplus merchandise. Even those merchants who gauged the market correctly and kept their inventories in line with sales were forced to slash their prices to meet the lower tags of overstocked competitors. These widespread markdowns cut deeply into their profits.

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending	$ Change Since	
	12/11/85	Week Ago	Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	185.105	+ 2.646	+17.955
Loans to Depository Inst.	.681	– .892	– 2.620
Float	1.566	+ .322	– .267
Total Reserve Bank Credit	201.499	+ 2.172	+17.818
Treasury Deposits with Federal Reserve Banks	2.565	+ .307	– .766
Currency in Circulation	194.607	+ .862	+13.798
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	125.661	– 1.513	+ 6.811
	12/4/85		
Member Bank Reserves:			
Total Reserves Held	45.232	+ .621	+ 6.268
Excess (Deficiency)	1.063	+ .162	+ .149
Net Borrowed Reserves	1.362	+ 1.117	+ 1.514
		% Change Since	
Monetary Aggregates †		Three Months Ago*	Year Ago
M1 (12/2/85)	626.1	+ 8.3‡	+ 11.7‡
M2 (November '85)	2,547.3	+ 5.3	+ 8.6
M3 (November '85)	3,190.6	+ 6.4	+ 7.8
Domestic Nonfinancial Debt (3rd Q'85)	6,523.1	+ 11.7	+ 13.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 12/13/85	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	6.95%	6.94%	6.98%
* Federal Agencies	7.49	7.60	7.76
* Municipal Notes—High Grade (46% Taxable Equivalent)	10.00	10.19	10.19
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.65	7.65	7.70

‡ Finance Company Paper—Prime	
5- 14 days	7.70%
15- 29 days	7.70
30- 59 days	7.70
60- 89 days	7.60
90-179 days	7.50
180-239 days	7.38
240-270 days	7.38

‡* Bankers' Acceptances	
Jan.	7.75%
Feb.	7.70
Mar.	7.60
Apr.	7.50
May	7.45
Jun.	7.40

‡ Industrial Paper—Prime	
30- 89 days	7.68%
90-120 days	7.60

†Federal Funds Effective Rate 7.85%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 3,916	$ 3,853	$ 3,695
Gross National Product (1972 Dollars)*	3rd Q'85	$ 1,689	$ 1,671	$ 1,645
Percent Change, Annual Rate	3rd Q'85	4.3	1.9	1.6
Change in Consumer Prices*	Oct '85	3.6%	2.4%	3.6%
Change in Producer Prices*	Nov '85n	9.6%	10.8%	3.6%
Civilian Employment (Thousands of Persons) †	Nov '85	107,927	107,867	105,932
Unemployment as % of Civilian Labor Force †	Nov '85	7.0%	7.1%	7.1%
Personal Income*	Oct '85	$ 3,221	$ 3,207	$ 3,079
Leading Indicators Composite Index (1967=100) †	Oct '85	171.1	170.6	164.2
Industrial Production Index (1977=100) †	Nov '85n	125.1	124.6r	123.4
Net Change in Consumer Installment Credit †	Oct '85n	$ 6.63	$ 11.53r	$ 5.63
U.S. Merchandise Trade Balance †	Oct '85	–$ 11.45	–$ 15.55	–$ 9.65
Plant and Equipment Expenditures*	4th Q'85	$387.40(a)	$389.54(a)	$368.29
Private Housing Starts (Thousands of Units)*	Oct '85	1,760	1,589	1,564
New Construction Expenditures*	Oct '85	$ 347.8	$ 346.1	$ 318.2
Total Business Inventories †	Oct '85n	$ 582.0	$ 578.9r	$ 568.8
Total Business Sales †	Oct '85n	$ 426.3	$ 429.0r	$ 414.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

This year, however, inventories are much leaner and most stores so far have avoided widespread price-cutting. In turn, this suggests that Christmas 1985 will be more profitable for retailers than last year. Although shoppers still can find special deals, these bargains are offered primarily on promotional items and have been carefully planned and priced to provide good-sized profits even after discounts.

Notwithstanding the absence of markdowns, consumers are not paying much more for their Holiday presents than they did last year. In the last 12 months, prices of consumer goods rose only 1.8 percent, the smallest increase in almost 20 years. In fact, prices of a number of products, such as some videocassette recorders and compact disc players, which are on the list of this year's hot-selling items, are lower today than a year ago. Other best-selling items vary from apparel, shoes and fashion accessories to jewelry, household goods, electronic gadgetry and toys. Merchandise with "Made in the U.S.A." labels are also selling well.

Consumers are clearly carrying heavier loads than just their Holiday packages at this time. The future of the current business expansion is also in their hands. Since personal consumption expenditures bulk so large in the GNP, accounting for about two-thirds of the overall economy, any retrenchment in consumer spending now could put a damper on business in 1986.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (11/27/85)	157,642	+ 282	– 1,255
New York City (12/4/85)	33,766	+ 308	– 605
Commercial Paper (12/4/85)	293,397	+ 3,206	+56,417

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (11/27/85)	254,966	+ 690	+ 5,226
New York City (12/4/85)	60,454	+ 1,218	– 3,579

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (11/27/85)	706,779	+ 239	+ 63,682
New York City (12/4/85)	158,234	+ 1,176	+ 11,236

Financial Markets

	Friday 12/13/85	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.19%	– .29	– 1.35
180-Day Bills†	7.31	– .38	– 1.55
Longest Bills†	7.46	– .42	– 1.95
Recent Issues:			
$8^{1}/_{2}$s 11/30/87	7.97	– .49	
$9^{3}/_{8}$s 9/30/89	8.48	– .52	
$9^{1}/_{2}$s 11/15/95	9.20	– .43	
$9^{7}/_{8}$s 11/15/15	9.53	– .36	
Municipals:			
Bond Buyer–20 Bond Index* (12/12/85)	8.42%	– .12	– 1.58
Blue List Total ($ Million)	$2,340	+$ 2	– $290
30-Day Visible Supply ($ Million)	$3,130	–$2,230	+ $976
Total	$5,470	–$2,228	+ $686
Corporates:			
Moody's Aa Composite (12/12/85)	10.68%	– .24	– 1.91
30-Day Visible Supply ($ Million)	$ 755	–$ 825	– $955
Stocks:			
Dow-Jones Averages:			
Industrials	1,535.21	+ 58.03	+ 359.30
Transportation	722.61	+ 29.02	+ 187.62
Utilities	168.80	+ 3.23	+ 24.21
65 Stocks	613.91	+ 21.95	+ 140.31
Standard and Poor's 500 Stocks	209.94	+ 6.95	+ 47.25
N.Y.S.E. Composite Index	120.83	+ 3.84	+ 26.91
N.Y.S.E. Avg. Daily Vol. for Week (000's)	165,484	+30,452	+ 82,220

* 46% Taxable equivalent 15.59%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 12/13/85	Week Ago
Overnight	7.81%	8.00%
1 month	8.00	8.19
3 month	7.88	8.13
6 month	7.88	8.13
1 year	8.00	8.31
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.09%	9.50%
Long Term (7 to 15 yrs.)	9.66	10.00

FOREIGN EXCHANGE SPOT RATES

New York Opening (12/13/85)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.01946	51.3800
Canada	.7196	1.3896
Denmark	.1096	9.1200
France	.1300	7.6950
Germany	.3976	2.5150
Italy	.0005833	1714.50
Japan	.004944	202.25
Mexico	.002153	464.50
Netherlands	.3530	2.8328
Switzerland	.4757	2.1023
U.K.	1.4420	.6935

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Foreign Exchange Expertise

We have become a preferred foreign exchange source for many major corporations. Through 24 key locations around the world, we trade virtually every currency and provide our customers with the latest in innovative foreign exchange services such as currency options. Manufacturers Hanover was named one of the three leading banks in foreign exchange forecasting, according to a recent Euromoney Corporate Finance poll.

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We are a primary U.S. Government Securities dealer and are regarded as a primary money market dealer. Our futures brokerage subsidiary provides the latest in trading and hedging services.

A Leader in Public Finance

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We draw on the traditional corporate finance skills of our experienced officer staff, as well as the depth of our customer base, to be a leader in structuring mergers and acquisitions, buyouts, project finance and venture capital.

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The Manufacturers Hanover Financial Digest

Weekly Commentary,
Selected Financial Data,
and Business Indicators

DECEMBER 23, 1985/DECEMBER 30, 1985
VOLUME XXII, NUMBER 46

Season's greetings
...and a HAPPY NEW YEAR to all!
1986

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270 Park Avenue, New York, N.Y. 10017

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

Reserve Bank Credit	Week Ending 12/18/85	$ Change Since Week Ago	$ Change Since Year Ago
U.S. Gov'ts and Agencies Owned Outright & RPs	186.528	+ 1.433	+19.620
Loans to Depository Inst.	1.001	+ .320	− 2.160
Float	1.163	− .400	− .168
Total Reserve Bank Credit	203.162	+ 1.667	+20.479
Treasury Deposits with Federal Reserve Banks	3.776	+ 1.211	+ .308
Currency in Circulation	194.760	+ .165	+13.348
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	125.935	+ .274	+ 4.774
	12/18/85		
Member Bank Reserves:			
Total Reserves Held	45.990	+ .754	+ 6.374
Excess (Deficiency)	.797	− .251	+ .271
Net Free Reserves	.480	+ 1.857	+ .411

Monetary Aggregates †		% Change Since Three Months Ago*	% Change Since Year Ago
M1 (12/9/85)	623.0	+ 8.1‡	+ 12.0‡
M2 (November '85)	2,547.4	+ 5.3	+ 8.6
M3 (November '85)	3,192.7	+ 6.4	+ 7.9
Domestic Nonfinancial Debt (3rd Q'85)	6,523.1	+ 11.7	+ 13.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 12/20/85	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	7.09%	7.08%	7.07%
* Federal Agencies	7.30	7.25	7.27
* Municipal Notes—High Grade (46% Taxable Equivalent)	11.11	10.65	10.42
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.65	7.65	7.70

‡ Finance Company Paper—Prime	
5- 14 days	7.80%
15- 29 days	7.83
30- 59 days	7.80
60- 89 days	7.75
90-179 days	7.63
180-239 days	7.50
240-270 days	7.50

‡* Bankers' Acceptances	
Jan.	7.80%
Feb.	7.65
Mar.	7.60
Apr.	7.60
May	7.55
Jun.	7.45

‡ Industrial Paper—Prime	
30- 89 days	7.70%
90-120 days	7.55

† Federal Funds	
Effective Rate	7.95%

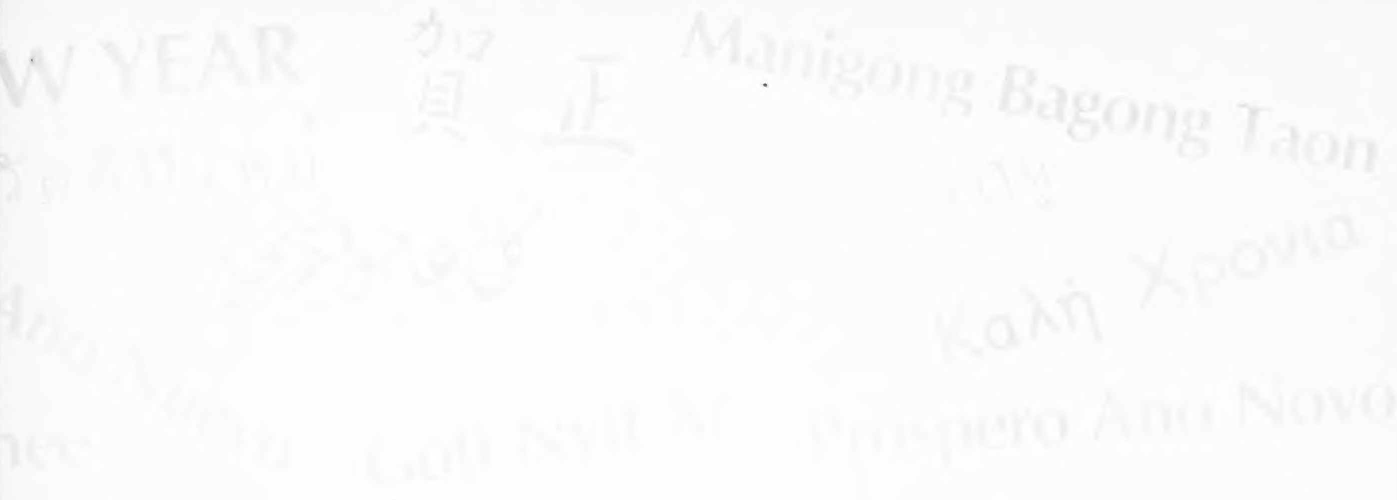
‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 4,017 r	$ 3,961 r	$ 3,812 r
Gross National Product (1982 Dollars)*	3rd Q'85	$ 3,584 r	$ 3,557 r	$ 3,510 r
Percent Change, Annual Rate	3rd Q'85	3.0 r	1.1 r	2.1 r
Change in Consumer Prices*	Nov '85n	7.2%	3.6%	2.4%
Change in Producer Prices*	Nov '85	9.6%	10.8%	3.6%
Civilian Employment (Thousands of Persons) †	Nov '85	107,927	107,867	105,932
Unemployment as % of Civilian Labor Force †	Nov '85	7.0%	7.1%	7.1%
Personal Income*	Oct '85	$ 3,221	$ 3,207	$ 3,079
Leading Indicators Composite Index (1967=100) †	Oct '85	171.1	170.6	164.2
Industrial Production Index (1977=100) †	Nov '85	125.1	124.6	123.4
Net Change in Consumer Installment Credit †	Oct '85	$ 6.63	$ 11.53	$ 5.63
U.S. Merchandise Trade Balance †	Oct '85	−$ 11.45	−$ 15.55	−$ 9.65
Plant and Equipment Expenditures*	1st Q'86n	$402.13(a)	$388.90(a) r	$371.16
Private Housing Starts (Thousands of Units)*	Nov '85n	1,547	1,761 r	1,600
New Construction Expenditures*	Oct '85	$ 347.8	$ 346.1	$ 318.2
Total Business Inventories †	Oct '85	$ 582.0	$ 578.9	$ 568.8
Total Business Sales †	Oct '85	$ 426.3	$ 429.0	$ 414.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.



Short Term Paper Outstanding
(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (12/4/85)	156,880	– 819	– 2,418
New York City (12/11/85)	34,018	+ 252	– 236
Commercial Paper (12/11/85)	292,642	– 764	+54,155

Bank Loans
(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (12/4/85)	256,426	+ 1,440	+ 5,221
New York City (12/11/85)	59,319	– 1,135	– 3,790

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (12/4/85)	708,982	+ 2,259	+ 56,567
New York City (12/11/85)	156,283	– 2,035	+ 11,799

Financial Markets

	Friday 12/20/85	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.32%	+ .13	– .68
180-Day Bills†	7.39	+ .08	– 1.06
Longest Bills†	7.51	+ .05	– 1.54
Recent Issues:			
$7\frac{7}{8}$s 12/31/87 (When Issued)	7.93	NA	
$8\frac{3}{8}$s 12/31/89 (When Issued)	8.34	NA	
$9\frac{1}{2}$s 11/15/95	8.99	– .21	
$9\frac{7}{8}$s 11/15/15	9.29	– .24	
Municipals:			
Bond Buyer–20 Bond Index* (12/19/85)	8.38%	– .04	– 1.55
Blue List Total ($ Million)	$2,136	–$ 204	+ $ 26
30-Day Visible Supply ($ Million)	$1,388	–$1,742	+ $293
Total	$3,524	–$1,946	+ $319
Corporates:			
Moody's Aa Composite (12/19/85)	10.48%	– .20	– 1.95
30-Day Visible Supply ($ Million)	$ 650	–$ 105	+ $150
Stocks:			
Dow-Jones Averages:			
Industrials	1,543.00	+ 7.79	+ 344.02
Transportation	711.26	– 11.35	+ 160.88
Utilities	174.96	+ 6.16	+ 28.16
65 Stocks	616.35	+ 2.44	+ 132.63
Standard and Poor's 500 Stocks	210.94	+ 1.00	+ 45.43
N.Y.S.E. Composite Index	121.32	+ .49	+ 25.76
N.Y.S.E. Avg. Daily Vol. for Week (000's)	153,646	–11,838	+ 34,950

* 46% Taxable equivalent 15.52%.

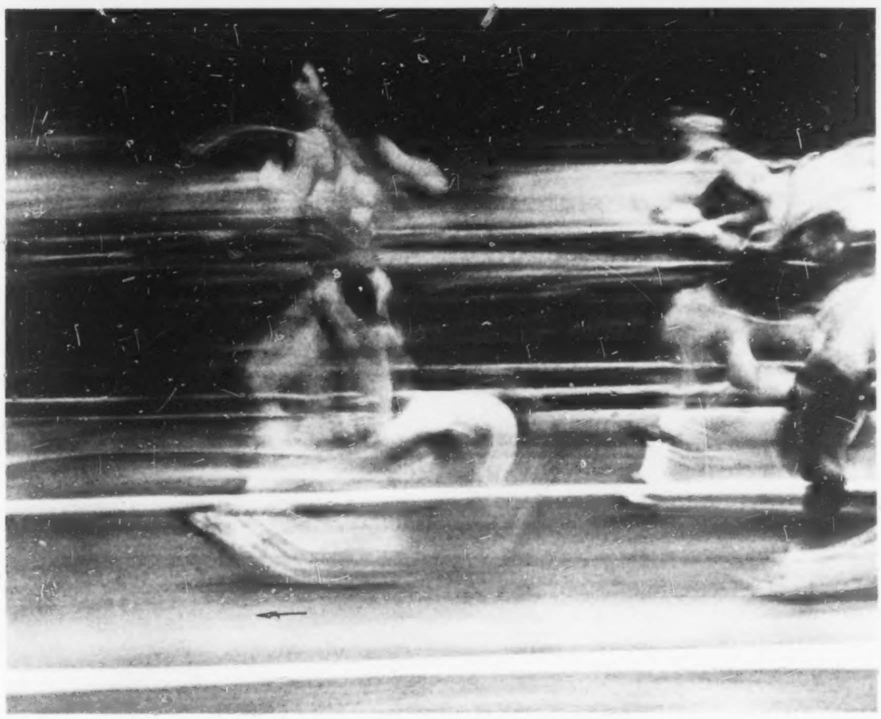
† Bond equivalent.

International Rates

	Friday 12/20/85	Week Ago
EURODOLLAR DEPOSIT RATES (bid)		
Overnight	7.63%	7.81%
1 month	7.94	8.00
3 month	7.94	7.88
6 month	7.88	7.88
1 year	8.00	8.00
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.00%	9.09%
Long Term (7 to 15 yrs.)	9.60	9.66

FOREIGN EXCHANGE SPOT RATES

New York Opening (12/20/85)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.01940	51.5500
Canada	.7151	1.3984
Denmark	.1095	9.1320
France	.1295	7.7225
Germany	.3975	2.5160
Italy	.0005828	1716.00
Japan	.004930	202.85
Mexico	.002195	455.50
Netherlands	.3528	2.8348
Switzerland	.4731	2.1138
U.K.	1.4220	.7032



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The Manufacturers
Hanover
Financial
Digest
Weekly Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, JANUARY 6, 1986
VOLUME XXIII, NUMBER 1

Rising Food And Energy Costs . . .

One of the most welcome developments accompanying the current economic expansion is the relatively low rate of inflation. Over the past 12 months, retail prices, as measured by the consumer price index (CPI), rose by only 3.6 percent. At the wholesale level, the producer price index (PPI) increased only 1.6 percent over the same period. But now, concerns over a newly rekindled inflation spiral are emerging, fueled by November's 0.6 percent month-over-month rise in the CPI and two consecutive large monthly jumps, 0.8 percent in November and 0.9 percent in October, in the PPI.

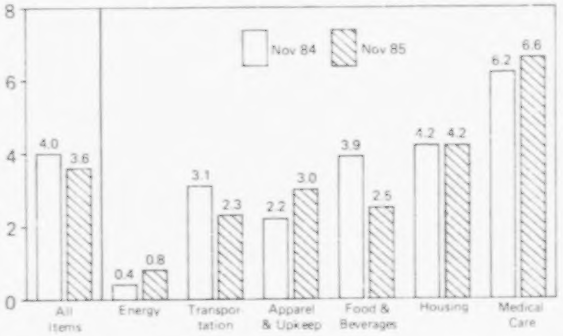
The 0.6 percent advance in the CPI was the largest rise in almost two years. It was double October's increase and triple that for each month from May through September. But this does not necessarily portend a major outburst of inflation. Higher food and energy costs were the main factors behind the recent advance in retail and wholesale prices and these increases are expected to be only short-lived. The impact of these two categories on the overall level of inflation can be seen by looking at a price index which excludes them. Without these two components, which account for almost one-third of the CPI, November's increase would be only 0.4 percent. For the PPI, the difference is even more dramatic, as the PPI excluding food and energy rose only 0.1 percent in November rather than 0.8 percent, month-over-month.

Food prices are probably of greatest concern to most people since about one-fifth of the average consumer's budget is devoted to purchases of food and beverages. Although this component was one of the largest contributors to November's uptick in inflation, it reflected volatility in livestock prices rather than a trend toward rapidly rising farm product prices. Meat prices in November rose 2.6 percent, compared with October, after falling in eight of the previous nine months. This rise was led by beef and veal prices, which rose 3.5 percent due to stepped-up slaughtering of herds earlier than usual this year as debt-strapped farmers tried to raise money to pay for spring planting costs.

. . . Do Not Spell . . .

Energy prices went up due to temporary shortages in gasoline and home-heating oil. These shortages were brought about by two factors. First, refiners had been keeping inventories of these products lean, anticipating that prices of crude oil would decline, and second, the early advent of severe winter weather in many parts of the country suddenly increased the demand for heating oil. Gasoline prices rose 1.4 percent in November, month-over-month, after dropping for four straight months, but home-heating oil prices rose a hefty 4.6 percent. However, neither food nor energy prices are expected to continue rising rapidly for long, given the general weakness in the farm economy and the recent declines in oil prices amid the disarray within the Organization of Petroleum Exporting Countries.

CONSUMER PRICE INDEX AND SELECTED COMPONENTS
(PERCENT CHANGE FROM A YEAR AGO)



In spite of the uptick in November, the 12-month increase in food and beverage prices is only 2.5 percent, well below the 3.9 percent jump posted in the previous 12-month period (see chart). For energy prices, the latest 12-month rise is 0.8 percent. While this is double the 0.4 percent gain in the previous 12 months, it is only a fraction of the double-digit increases seen in the early 1980s. Apparel and upkeep prices and medical care costs are increasing somewhat faster in the latest 12-month period than in the immediately preceding 12 months, while transportation costs are increasing more slowly and housing costs have risen at the same pace over these two periods.

Manufacturers Hanover
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. . . An Early End To Low Inflation

One reason to be wary about the inflation outlook is the lower value of the dollar compared with foreign currencies, and its possible effect on the prices of consumer goods. Inflation trends in the two broad categories of consumer purchases, goods and services, are strikingly different (Financial Digest—October 28, 1985). The 12-month rate of rise in prices of goods—2.3 percent—has been running at less than half of the rate of rise in services' prices. The main reason for this difference is lower-priced imports due to the strong dollar and lower labor costs in many areas overseas. This has forced domestic goods producers to hold down price increases in order to be more competitive. Services are not generally imported and therefore, the providers of these services have not faced the same price competition.

But since its late February peak, the value of the dollar on a trade-weighted basis has dropped almost 25 percent. Using the rule of thumb that each ten percent reduction in the value of the dollar would increase the overall price level by about one percent within two years—as foreign product prices rise in terms of dollars, allowing domestic producers to raise prices—there is the possibility of an increase in the rate of inflation from around 3.5 percent to six percent throughout the next two years. This increase in inflation would reflect the rate of rise in

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 12/25/85	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	187.614	+ 1.086	+18.390
Loans to Depository Inst.	.948	– .053	– .896
Float	1.347	+ .210	+ .120
Total Reserve Bank Credit	204.576	+ 1.455	+20.572
Treasury Deposits with Federal Reserve Banks	3.577	– .199	– .092
Currency in Circulation	195.964	+ 1.204	+13.151
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	125.161	+ .774	+ 3.839
	12/18/85		
Member Bank Reserves:			
Total Reserves Held	45.983	+ .740	+ 6.367
Excess (Deficiency)	.841	– .197	+ .315
Net Free Reserves	.524	+ 1.911	+ .455
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates †			
M1 (12/16/85)	622.6	+ 8.4‡	+ 12.2‡
M2 (November '85)	2,547.1	+ 5.3	+ 8.6
M3 (November '85)	3,194.4	+ 6.6	+ 7.9
Domestic Nonfinancial Debt (3rd Q'85)	6,523.1	+ 11.7	+ 13.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 1/3/86	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	7.08%	7.11%	7.10%
* Federal Agencies	7.25	7.25	7.28
* Municipal Notes—High Grade (46% Taxable Equivalent)	10.37	10.00	10.65
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.77	7.75	7.75

‡Finance Company Paper—Prime	
5- 14 days	7.75%
15- 29 days	7.75
30- 59 days	7.80
60- 89 days	7.65
90-179 days	7.62
180-239 days	7.60
240-270 days	7.60

‡* Bankers' Acceptances	
Feb.	7.80%
Mar.	7.70
Apr.	7.60
May	7.55
Jun.	7.50
Jul.	7.45

‡Industrial Paper—Prime	
30- 89 days	7.70%
90-120 days	7.55

†Federal Funds Effective Rate 8.30%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 4,017	$ 3,961	$ 3,812
Gross National Product (1982 Dollars)*	3rd Q'85	$ 3,584	$ 3,557	$ 3,510
Percent Change, Annual Rate	3rd Q'85	3.0	1.1	2.1
Change in Consumer Prices*	Nov '85	7.2%	3.6%	2.4%
Change in Producer Prices*	Nov '85	9.6%	10.8%	3.6%
Civilian Employment (Thousands of Persons)†	Nov '85	107,927	107,867	105,932
Unemployment as % of Civilian Labor Force†	Nov '85	7.0%	7.1%	7.1%
Personal Income*	Nov '85n	$ 3,345	$ 3,326r	$ 3,184r
Leading Indicators Composite Index (1967=100)†	Nov '85n	171.5	171.3r	165.1
Industrial Production Index (1977=100) †	Nov '85	125.1	124.6	123.4
Net Change in Consumer Installment Credit †	Oct '85	$ 6.63	$ 11.53	$ 5.63
U.S. Merchandise Trade Balance †	Nov '85n	–$ 13.68	–$ 11.45	–$ 10.22
Plant and Equipment Expenditures*	1st Q'86	$402.13(a)	$388.98(a)	$371.16
Private Housing Starts (Thousands of Units)*	Nov '85	1,547	1,761	1,600
New Construction Expenditures*	Nov '85n	$ 348.2	$ 346.3r	$ 313.1
Total Business Inventories †	Oct '85	$ 582.0	$ 578.9	$ 568.8
Total Business Sales †	Oct '85	$ 426.3	$ 429.0	$ 414.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

goods prices brought up to the rate experienced by services. This has not occurred for a prolonged period of time since 1979, just before the dollar reached its low point on a trade-weighted basis. But some foreign producers may not raise prices. Instead they may choose to cut into their profit margins rather than risk losing their market share to U.S. producers, making the effect of the lower-valued dollar on inflation less certain than in the past.

The dramatic slowdown in the pace of U.S. wage gains has been crucial to keeping inflation in check, since labor costs represent two-thirds of business operating costs. Average hourly earnings of nonfarm production workers increased at an extremely low pace in the third quarter of this year. This slowdown shows up in the rate of rise in the Commerce Department's index of unit labor costs. For the manufacturing sector, unit labor costs have actually fallen for two consecutive quarters, bringing the increase over the past four quarters to only 2.1 percent. The index of unit labor costs for all nonfarm business rose somewhat faster, posting a four-quarter gain of 3.3 percent. The fact that workers have been less worried about inflation and more concerned about job security has helped keep labor costs down, but this could change as 1986 unfolds and the effects of a lower-valued dollar are felt by consumers and businesses alike.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (12/18/85)	158,178	– 34	– 3,182
New York City (12/18/85)	34,440	+ 422	– 140
Commercial Paper (12/18/85)	293,161	+ 552	+54,632

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (12/18/85)	254,985	+ 855	+ 2,899
New York City (12/18/85)	58,927	– 375	– 4,808

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (12/18/85)	714,690	+ 9,111	+ 54,572
New York City (12/18/85)	159,014	+ 2,784	+ 9,144

Financial Markets

	Friday 1/3/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.29%	+ .11	– .76
180-Day Bills†	7.48	+ .11	– 1.12
Longest Bills†	7.63	+ .08	– 1.50
Recent Issues:			
$7\frac{7}{8}$s 12/31/87	8.04	+ .06	
$8\frac{3}{8}$s 12/31/89	8.41	+ .02	
$9\frac{1}{2}$s 11/15/95	9.05	+ .07	
$9\frac{7}{8}$s 11/15/15	9.29	+ .02	
Municipals:			
Bond Buyer–20 Bond Index* (1/2/86)	8.33%	– .03	– 1.54
Blue List Total ($ Million)	$1,780	– $335	– $ 31
30-Day Visible Supply ($ Million)	$ 537	– $499	– $1,571
Total	$2,317	– $834	– $1,602
Corporates:			
Moody's Aa Composite (1/2/86)	10.69%	+ .27	– 1.86
30-Day Visible Supply ($ Million)	$ 710	+ $ 60	+ $ 360
Stocks:			
Dow-Jones Averages:			
Industrials	1,549.20	+ 6.20	+ 364.24
Transportation	702.99	– 5.46	+ 149.96
Utilities	175.88	+ 3.79	+ 29.34
65 Stocks	616.50	+ 2.30	+ 135.57
Standard and Poor's 500 Stocks	210.88	+ 1.27	+ 47.20
N.Y.S.E. Composite Index	121.50	+ .88	+ 26.90
N.Y.S.E. Avg. Daily Vol. for Week (000's)	102,240	+19,790	+ 23,630

* 46% Taxable equivalent 15.43%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 1/3/86	Week Ago
Overnight	8.00%	7.81%
1 month	7.90	8.25
3 month	8.00	8.00
6 month	8.00	8.00
1 year	8.06	8.00
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	8.85%	8.85%
Long Term (7 to 15 yrs.)	9.60	9.60

FOREIGN EXCHANGE SPOT RATES

New York Opening (1/3/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.01990	50.2500
Canada	.7124	1.4038
Denmark	.1116	8.9600
France	.1325	7.5450
Germany	.4062	2.4618
Italy	.0005959	1678.00
Japan	.004942	202.33
Mexico	.002286	437.50
Netherlands	.3608	2.7715
Switzerland	.4838	2.0670
U.K.	1.4445	.6923

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The Manufacturers Hanover Financial Digest
Weekly Commentary, Selected Financial Data, and Business Indicators

MONDAY, JANUARY 13, 1986
VOLUME XXIII, NUMBER 2

Labor Talks In 1986 Will Center . . .

Helped by the decline in December's unemployment rate to 6.9 percent, the jobless rate for all of 1985 was the lowest for any year since 1980. With over 108 million people working in December, America's labor force posted another record high for total employment and saw almost three million jobs added to nonfarm payrolls during the year. More than one million of those jobs were created in the services industry, and another 812,000 were added by the retail and wholesale trade sector. Employment fell, however, in the manufacturing and mining industries.

Given these divergent trends between the goods-producing and service-producing labor markets, 1986 looks to be another year of moderate wage increases for most of those workers whose unions will meet management at bargaining tables this year. Certainly, the loss of over 200,000 jobs in the nation's factories and mines in 1985 will weaken the bargaining positions of the aluminum, steel and farm machinery workers whose contracts expire in 1986. On the other hand, the healthy gains in state and local government jobs, coupled with budget surpluses in many states, might well help those 738,000 public workers covered by new labor accords this year.

To be sure, expectations of higher inflation and a lower exchange rate for the U.S. dollar should benefit, to some extent, all of the 3.8 million workers negotiating new collective bargaining settlements in 1986. However, gone are the days of the late 1970s and early 1980s when unions bargained for, and won, double-digit pay hikes for their members. In fact, 1986 is expected to follow 1985 as another year when the average wage increase for union workers falls below the rate of inflation. A shrinking membership base and high levels of unemployment have caused unions to become less aggressive bargainers than in the past. In 1985, strike activity fell to its lowest level on record with only 51 work stoppages. In the 1970s, unions organized an average of 289 strikes per year.

During the first nine months of 1985, major collective bargaining agreements covering 1,000 or more workers called for an average pay increase of 2.3 percent in the first year and 2.9 percent annually during the life of the contract. In contrast, the inflation rate during the same nine months was three percent. Moreover, 37 percent of the 1.6 million workers covered by the contracts signed between January and September agreed to either no wage change or to pay decreases in the first contract year.

Another important trend is the growing frequency of "back-loading" wage increases. This means wage adjustments are lower in the first year of a contract than in later years—a practice almost unheard of before 1983. During the first nine months of 1985, however, 726,000 workers, or 45 percent of those covered by new contracts, agreed to back-loaded settlements. The majority of these contracts were in the apparel, electrical machinery and construction industries.

. . . On Boosting Job Security . . .

It is clear that unions were more concerned about job security than hefty pay gains in 1985 especially in the ever shrinking manufacturing sector. This concern will not lessen in 1986 when labor and management bring differing contract objectives to the bargaining table. For management, the main goal will be holding down labor costs which account for two-thirds of all production expenses in the manufacturing sector. One way to achieve this is through the dismantling of cost-of-living adjustments (COLA) that tie automatic wage hikes to increases in the consumer price index or some other inflation measure.

Even now, COLA clauses are losing popularity. During the first nine months of 1985, they were dropped in contracts covering 327,000 workers, thus reducing the proportion of workers with COLA adjustments from 57 percent to 50 percent. Other objectives for employers will be the adoption of a two-tier wage system which would lower pay scales offered to new workers while the existing work force continues to receive the old wage package, and lump-sum payments tied to company or production-unit performance instead of the usual annual percentage wage jumps. This pay method has the advantages of linking pay with company earnings

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and avoiding any increases in costly fringe benefits.

Unions, on the other hand, will want contracts to include assurances of job security. Other labor demands may be drawn from a 1985 pact reached in the auto industry. Although described as a "special case" agreement between the United Auto Workers and one of the domestic manufacturers in an attempt to battle the cost advantages of foreign small car producers, this innovative contract possesses new approaches to labor relations which may influence negotiations in all industries in the future. These provisions include permanent job security, elimination of time clocks and greater labor participation in company decision-making.

In the months to come, public attention will likely focus on talks in the steel and communications industries. Unlike previous bargaining rounds when the steel companies formed a consortium to negotiate an industrywide contract, this time the United Steelworkers will negotiate separately with each of six major steel companies. For the Communications Workers of America, deregulation within the telephone communications industry will also change that union's bargaining pattern when the contract covering 500,000 of its members expires in August.

. . . And Holding Down Employment Costs

The retrenchment of unions has softened the upward trend in employment costs in industries with a strong union presence. Whereas in the 12 months ending in December 1981, the construction

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending	$ Change Since	
		Week Ago	Year Ago
Reserve Bank Credit	1/8/86		
U.S. Gov'ts and Agencies Owned Outright & RPs	187.878	– 3.243	+34.511
Loans to Depository Inst.	.612	– 1.115	– 1.450
Float	1.126	– .519	– .077
Total Reserve Bank Credit	204.628	– 2.783	+18.135
Treasury Deposits with Federal Reserve Banks	4.140	– 1.505	+ .650
Currency in Circulation	196.315	– .962	+13.530
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	126.112	+ .488	+10.127
Member Bank Reserves:	1/1/86		
Total Reserves Held	47.240	+ 1.269	+ 6.027
Excess (Deficiency)	1.325	+ .495	+ .118
Net Free Reserves	.459	– .054	+ .444
		% Change Since	
Monetary Aggregates †		Three Months Ago*	Year Ago
M1 (12/30/85)	624.7	+ 8.2‡	+ 11.7‡
M2 (November '85)	2,547.0	+ 5.2	+ 8.6
M3 (November '85)	3,194.5	+ 6.6	+ 7.9
Domestic Nonfinancial Debt (3rd Q'85)	6,523.1	+ 11.7	+ 13.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 1/10/86	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	7.15%	7.26%	7.27%
* Federal Agencies	7.42	7.45	7.42
* Municipal Notes–High Grade (46% Taxable Equivalent)	9.63	9.72	10.19
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market–Prime	7.80	7.91	7.95

‡Finance Company Paper–Prime		‡* Bankers' Acceptances	
5- 14 days	7.60%	Feb.	7.75%
15- 29 days	7.70	Mar.	7.70
30- 59 days	7.75	Apr.	7.65
60- 89 days	7.75	May	7.65
90-179 days	7.67	Jun.	7.65
180-239 days	7.50	Jul.	7.60
240-270 days	7.50		

‡Industrial Paper–Prime			
30- 89 days	7.73%	†Federal Funds	
90-120 days	7.60	Effective Rate	7.85%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period at End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 4,017	$ 3,961	$ 3,812
Gross National Product (1982 Dollars)*	3rd Q'85	$ 3,584	$ 3,557	$ 3,510
Percent Change, Annual Rate	3rd Q'85	3.0	1.1	2.1
Change in Consumer Prices*	Nov '85	7.2%	3.6%	2.4%
Change in Producer Prices*	Dec '85n	4.8%	9.6%	0.0%
Civilian Employment (Thousands of Persons) †	Dec '85n	108,206	107,969r	106,248r
Unemployment as % of Civilian Labor Force †	Dec '85n	6.9%	7.0%	7.2%
Personal Income*	Nov '85	$ 3,345	$ 3,326	$ 3,184
Leading Indicators Composite Index (1967=100) †	Nov '85	171.5	171.3	165.1
Industrial Production Index (1977=100) †	Nov '85	125.1	124.6	123.4
Net Change in Consumer Installment Credit †	Oct '85	$ 6.63	$ 11.53	$ 5.63
U.S. Merchandise Trade Balance †	Nov '85	–$ 13.68	–$ 11.45	–$ 10.22
Plant and Equipment Expenditures*	1st Q'86	$402.13(a)	$388.98(a)	$371.16
Private Housing Starts (Thousands of Units)*	Nov '85	1,547	1,761	1,600
New Construction Expenditures*	Nov '85	$ 348.2	$ 346.3	$ 313.1
Total Business Inventories †	Oct '85	$ 582.0	$ 578.9	$ 568.8
Total Business Sales †	Oct '85	$ 426.3	$ 429.0	$ 414.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

and durable manufacturing sectors saw wage and salary expenses skyrocket 8.8 percent and 9.2 percent respectively, in the 12 months ending in September 1985, the increases had dwindled to respective rates of 2.6 and 4.2 percent. In comparison, at the end of the third quarter, the industry with the highest yearly increase, 7.6 percent, was the finance, insurance and real estate sector where unionized employees account for only three percent of the work force.

Even a small boost in wages, however, can be detrimental to a company if it is not accompanied by a similar rise in output. Here, manufacturing performed better than the business sector as a whole. While productivity in nonfarm businesses rose 2.1 percent at a seasonally adjusted annual rate in the third quarter of 1985, manufacturing posted a 3.7 percent increase. Moreover, since output per hour outpaced compensation per hour in manufacturing, unit labor costs actually declined during the second and third quarters of 1985.

Historically, wage increases won by unions have affected the salary hikes of nonunion workers. However, the economy's change in emphasis from goods production to services has diminished this relationship. Since the end of 1983, year-over-year percentage wage increases for nonunion employees have surpassed those gained by union workers. What is more, while some experts predict union wages may increase about 3½ percent in 1986, white-collar, nonunion employees may find their paychecks rising between 4½ and six percent this year.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (12/25/85)	159,753	+ 1,530	– 2,036
New York City (1/1/86)	37,247	+ 2,382	+ 1,848
Commercial Paper (12/31/85)	293,876	– 940	+60,669

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (12/25/85)	255,090	+ 135	+ 2,198
New York City (1/1/86)	59,398	+ 853	– 3,252

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (12/25/85)	717,536	+ 3,006	+ 55,665
New York City (1/1/86)	157,950	– 1,374	+ 11,593

Financial Markets

	Friday 1/10/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.42%	+ .13	– .61
180-Day Bills†	7.68	+ .20	– .83
Longest Bills†	7.82	+ .19	– 1.28
Recent Issues:			
$7^{7}/_{8}$s 12/31/87	8.26	+ .22	
$8^{3}/_{8}$s 12/31/89	8.69	+ .28	
$9^{1}/_{2}$s 11/15/95	9.30	+ .25	
$9^{7}/_{8}$s 11/15/15	9.47	+ .18	
Municipals:			
Bond Buyer–20 Bond Index* (1/9/86)	8.04%	– .29	– 1.56
Blue List Total ($ Million)	$1,379	– $401	– $ 3
30-Day Visible Supply ($ Million)	$ 609	+ $ 72	– $927
Total	$1,988	– $329	– $930
Corporates:			
Moody's Aa Composite (1/9/86)	10.38%	– .31	– 2.05
30-Day Visible Supply ($ Million)	$1,185	+ $475	+ $624
Stocks:			
Dow-Jones Averages:			
Industrials	1,513.53	– 35.67	+ 295.44
Transportation	686.97	– 16.02	+ 111.45
Utilities	172.75	– 3.13	+ 25.49
65 Stocks	602.83	– 13.67	+ 109.22
Standard and Poor's 500 Stocks	205.96	– 4.92	+ 38.05
N.Y.S.E. Composite Index	118.82	– 2.68	+ 21.83
N.Y.S.E. Avg. Daily Vol. for Week (000's)	146,602	+44,362	+ 44,468

* 46% Taxable equivalent 14.89%.

† Bond equivalent.

International Rates

	Friday 1/10/86	Week Ago
EURODOLLAR DEPOSIT RATES (bid)		
Overnight	7.75%	8.00%
1 month	8.19	7.90
3 month	8.19	8.00
6 month	8.25	8.00
1 year	8.44	8.06
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.20%	8.85%
Long Term (7 to 15 yrs.)	9.70	9.60

FOREIGN EXCHANGE SPOT RATES

New York Opening (1/10/86)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.0199	50.1500
Canada	.7161	1.3965
Denmark	.1124	8.8975
France	.1325	7.5475
Germany	.4067	2.4590
Italy	.0005972	1674.50
Japan	.004943	202.30
Mexico	.002446	408.80
Netherlands	.3609	2.7710
Switzerland	.4789	2.0880
U.K.	1.4535	.6880

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The Manufacturers Hanover Financial Digest

Economic Commentary,
Selected Financial Data,
and Business Indicators

FRIDAY, JANUARY 17, 1986
VOLUME XXIII, NUMBER 3

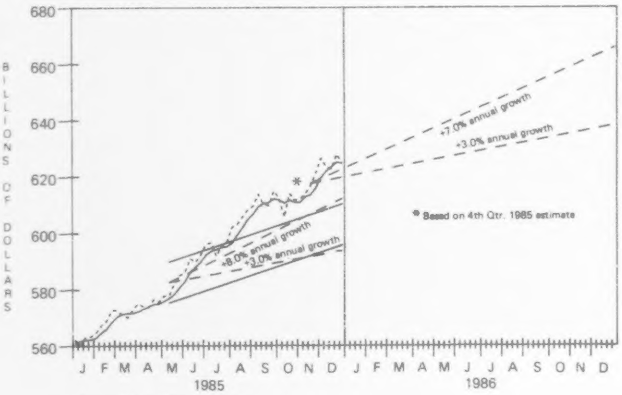
Great Expectations . . .

The likelihood of some upbeat economic statistics in coming weeks has prompted a decided reversal of fortunes in the credit markets—sending bond prices lower and yields somewhat higher. To a large extent, this development reflected the growing belief among market participants that if the economy is brightening, then prospects for a further easing of monetary policy are dimming, if not disappearing altogether. However, Fed policy actions have failed to live up to the most bullish of market expectations for quite some time (Financial Digest—December 2, 1985), not surprising when you consider the still sizable overrun in M1 money supply growth and concerns that too rapid a dollar decline in the foreign exchange markets could touch off another round of accelerating inflation rates. Since these concerns have not abated to any great extent, monetary policy initiatives will probably remain on hold for the time being, with the central bank encouraging neither higher nor lower interest rates.

Perhaps the most important factor behind the abrupt shift in market sentiment has been the course of recent business developments. With payroll employment expanding by a hefty 320,000 in December—or some 25 percent better than the preceding five-month average—and the unemployment rate sinking below seven percent, the ingredients for a bond market retreat began to fall into place. Since these numbers tend to act as leading indicators of trends in industrial production, capacity utilization and personal incomes growth, good-sized employment gains would suggest not only good-sized gains in these other business statistics, but also would enhance the likelihood that the 3.2 percent, fourth quarter "flash" estimate of gross national product growth was on the low side. Thus, with the economy seemingly emerging from its recent doldrums, and even the hard-pressed manufacturing sector enjoying some modest employment and production gains, the need for more monetary stimulation, at this time at least, would appear to have diminished.

Such trends do not, however, preclude ease forever, or suggest any near-term moves toward restraint—however modest. For one thing, some of the glow associated with December's statistics could fade. Nagging doubts persist regarding the sustainability of today's robust consumer spending levels; the solid retail sales gain posted last month, for instance, could be reversed if either consumer confidence ebbs or households aggressively initiate steps to rebuild depleted savings balances.

MONEY SUPPLY, M1
FOUR-WEEK MOVING AVERAGE (LINE) VS. WEEKLY FIGURES (DOT)



Source: Federal Reserve Board; MH

. . . Of More Monetary Ease . . .

What is more, the outlook for business capital spending remains clouded, if for no other reason that the fact that capacity utilization rates nationwide still stand nearly six full percentage points below those usually prevailing at this stage of the business cycle. Add to this the ongoing challenge of global competition to domestic industry and the uncertainty associated with proposed tax reform legislation, and it appears likely that capital spending will be lackluster this year—as recent surveys suggest. In fact, while GNP growth could perk up this year, it will be due mostly to stepped-up business inventory spending and a bottoming out of the trade deficit, not to a sustained upturn in final demand—two slim pillars on which to rest the fourth year of today's business expansion. But for now, the emergence of stronger economic statistics has given pause to further easing initiatives.

Money supply and Federal budget developments as well point toward a steady monetary policy course.

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As the new year unfolds, the Fed finds itself with an M1 money number standing some $12½ billion above 1985's upper growth target—not to mention slightly above 1986's seven percent upper growth target. Although M1 can expand by about $3 billion monthly and still end the year within target, since this year's growth will be starting from a large $5 billion average monthly increase in 1985, the Fed will undoubtedly be very wary of allowing once again large overshoots of its money growth targets. Even the growth of the broader money measures, M2 and M3, while within target, has picked up recently, a negative development which suggests a degree of caution on the part of the policymakers before taking steps which could stimulate additional money growth.

Other concerns abound as well. The government's estimate that the fiscal 1986 Federal budget deficit could hit a record $220 billion, together with legal challenges to the constitutionality of the Gramm-Rudman budget balancing bill, have heightened investor worries that the momentum toward putting in place a credible deficit reduction program could be slipping away. This would suggest that Washington's financial profligacy, and borrowing requirements, are not going to recede anytime soon, keeping the heat on the debt markets. For the monetary authorities, it implies that the need to loosen, if fiscal policy is tightened, has faded as well.

. . . Appear Dashed For Now

While business trends, money supply developments

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 1/15/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	188.911	+ 1.033	+40.281
Loans to Depository Inst.	.615	+ .003	– .585
Float	.581	– .545	– .083
Total Reserve Bank Credit	205.173	+ .545	+21.421
Treasury Deposits with Federal Reserve Banks	5.032	+ .892	+ 1.569
Currency in Circulation	194.049	– 2.266	+13.457
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	125.691	– .821	+ 7.509
	1/15/86		
Member Bank Reserves:			
Total Reserves Held	48.336	+ 1.091	+ 6.910
Excess (Deficiency)	1.252	– .078	+ .618
Net Free Reserves	1.109	+ .645	+ .442
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates †			
M1 (1/6/86)	628.5	+ 9.0‡	+ 11.6‡
M2 (December '85)	2,563.1	+ 5.4	+ 8.1
M3 (December '85)	3,213.5	+ 5.6	+ 7.3
Domestic Nonfinancial Debt (3rd Q'85)	6,523.1	+ 11.7	+ 13.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 1/17/86	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	7.07%	7.18%	7.23%
* Federal Agencies	7.38	7.40	7.38
* Municipal Notes—High Grade (46% Taxable Equivalent)	10.19	9.63	10.19
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.82	7.82	7.87

‡Finance Company Paper—Prime	
5- 14 days	7.65%
15- 29 days	7.75
30- 59 days	7.80
60- 89 days	7.75
90-179 days	7.70
180-239 days	7.65
240-270 days	7.65

‡* Bankers' Acceptances	
Feb.	7.70%
Mar.	7.70
Apr.	7.65
May	7.65
Jun.	7.65
Jul.	7.60

‡Industrial Paper—Prime	
30- 89 days	7.73%
90-120 days	7.60

†Federal Funds Effective Rate 7.85%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'85	$ 4,017	$ 3,961	$ 3,812
Gross National Product (1982 Dollars)*	3rd Q'85	$ 3,584	$ 3,557	$ 3,510
Percent Change, Annual Rate	3rd Q'85	3.0	1.1	2.1
Change in Consumer Prices*	Nov '85	7.2%	3.6%	2.4%
Change in Producer Prices*	Dec '85	4.8%	9.6%	0.0%
Civilian Employment (Thousands of Persons) †	Dec '85	108,206	107,969	106,248
Unemployment as % of Civilian Labor Force †	Dec '85	6.9%	7.0%	7.2%
Personal Income*	Nov '85	$ 3,345	$ 3,326	$ 3,184
Leading Indicators Composite Index (1967=100) †	Nov '85	171.5	171.3	165.1
Industrial Production Index (1977=100) †	Dec '85n	126.0	125.1	123.3
Net Change in Consumer Installment Credit †	Nov '85n	$ 4.88	$ 8.13r	$ 6.08
U.S. Merchandise Trade Balance †	Nov '85	–$ 13.68	–$ 11.45	–$ 10.22
Plant and Equipment Expenditures*	1st Q'86	$402.13(a)	$388.98(a)	$371.16
Private Housing Starts (Thousands of Units)*	Dec '85n	1,840	1,566r	1,630
New Construction Expenditures*	Nov '85	$ 348.2	$ 346.3	$ 313.1
Total Business Inventories †	Nov '85n	$ 583.4	$ 582.2r	$ 571.2
Total Business Sales †	Nov '85n	$ 432.3	$ 426.0r	$ 417.6

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

and the persistence of 12-digit Federal budget deficits all indicate a steady monetary posture, foreign exchange market developments probably do too—at least for now. The Group of Five major industrial nations (G-5) has so far been successful in dampening the dollar's external value, but they may not want this process to be carried too far, too fast. For one thing, if a cut in the discount rate, for example, accelerated the dollar's descent, it could have disturbing implications for our inflation rate. For another, the overseas participants in G-5 undoubtedly have their own reasons for fearing such a development, since it would tend to enhance U.S. global competitiveness at their exporters' expense. Thus, any policy loosening would probably be undertaken only in close cooperation with our overseas partners.

But there may be another good reason why the Fed may wish to postpone another round of ease. This is because if the pace of business picks up decidedly here while inflation rates are low and growth overseas remains lackluster, the dollar may well begin to strengthen again in the foreign exchange markets. Rather than move toward restraint, monetary policy may have to be eased, in order to forestall another sustained ascent of the dollar. If so, the Fed may well need just such ammunition as a discount rate cut later this year.

The next issue will be dated February 3.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (1/1/86)	164,139	+ 4,367	+ 3,428
New York City (1/8/86)	37,289	– 57	+ 2,281
Commercial Paper (1/8/86)	296,252	+ 2,343	+60,259

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (1/1/86)	260,200	+ 4,955	+ 6,969
New York City (1/8/86)	59,649	+ 101	– 2,712

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (1/1/86)	726,566	+ 8,866	+ 61,590
New York City (1/8/86)	162,268	+ 4,894	+ 18,370

Financial Markets

	Friday 1/17/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	7.33%	– .09	– .62
180-Day Bills†	7.58	– .10	– .77
Longest Bills†	7.75	– .07	– 1.20
Recent Issues:			
$7\frac{7}{8}$s 12/31/87	8.17	– .09	
$8\frac{3}{8}$s 12/31/89	8.59	– .10	
$9\frac{1}{2}$s 11/15/95	9.22	– .08	
$9\frac{7}{8}$s 11/15/15	9.40	– .07	
Municipals:			
Bond Buyer–20 Bond Index* (1/16/86)	8.10%	+ .06	– 1.41
Blue List Total ($ Million)	$1,438	+ $ 59	+ $184
30-Day Visible Supply ($ Million)	$ 945	+ $336	+ $514
Total	$2,383	+ $395	+ $698
Corporates:			
Moody's Aa Composite (1/16/86)	10.57%	+ .19	+ 1.06
30-Day Visible Supply ($ Million)	$1,310	+ $125	+ $790
Stocks:			
Dow-Jones Averages:			
Industrials	1,536.70	+ 23.17	+ 309.34
Transportation	716.64	+ 29.67	+ 138.92
Utilities	172.75	–0–	+ 25.21
65 Stocks	615.02	+ 12.19	+ 117.87
N.Y.S.E. Composite Index	120.33	+ 1.51	+ 21.29
N.Y.S.E. Avg. Daily Vol. for Week (000's)	149,610	+ 3,008	+ 22,734

* 46% Taxable equivalent 15.00%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 1/17/86	Week Ago
Overnight	7.75%	7.75%
1 month	8.06	8.19
3 month	8.06	8.19
6 month	8.06	8.25
1 year	8.25	8.44
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.25%	9.20%
Long Term (7 to 15 yrs.)	9.80	9.70

FOREIGN EXCHANGE SPOT RATES

New York Opening (1/17/86)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.01987	50.3300
Canada	.7135	1.4015
Denmark	.1107	9.0345
France	.1322	7.5650
Germany	.4057	2.4650
Italy	.0005951	1680.50
Japan	.004938	202.50
Mexico	.002205	453.50
Netherlands	.3601	2.7770
Switzerland	.4789	2.0880
U.K.	1.4360	.6964

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Economic Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, FEBRUARY 3, 1986

VOLUME XXIII, NUMBER 4

Lower Oil Prices . . .

January's economic events were dominated by news of a sharp decline in crude oil prices and speculation on what such a development implies for the U.S. and for other economies. Despite an initial chorus of negativism, lower oil prices will turn out to be a welcome tonic for global growth. The importance of oil to the world's economic health is so great that any significant change in prices can contribute to a decline or an expansion of real output and to a rise or fall in the rate of inflation. While it is still too early to assess at what level oil prices will stabilize and what effect the lower oil-price structure will have on the financial situation in parts of the U.S. and elsewhere, there is little doubt that lower oil prices will contribute to global economic growth while putting a damper on inflation and on interest rates. That spells particularly good news for the non-oil producing developing countries which have suffered from high energy costs and lower demand for their commodities because of lackluster economic growth in the industrialized nations.

. . . Enhance The Business Outlook . . .

The drop in oil prices also brightens the U.S. business outlook at a time when the recovery seems to be losing some of its steam. According to the Commerce Department, the nation's output of goods and services rose at an inflation-adjusted annual rate of only 2.4 percent in the final quarter of 1985, 0.8 percentage points lower than reported in the so-called "flash" GNP estimate a month earlier. What is more, this modest growth was accompanied by higher inflation. The GNP price deflator—the broadest measure of inflation—was revised to a 3.3 percent annual rate of rise for the October-December period, compared with the 2.9 percent annual rate of increase in the preceding three months.

The primary factor behind the downward revision of GNP growth in the fourth quarter was the continuing surge in real imports which grew 13 percent at an annual rate during that period, suggesting that the dollar's decline has yet to help increase the share of U.S. demand satisfied by domestic producers. Because of this continuing leakage of domestic demand abroad, and despite a healthy eight percent rise in U.S. real exports—which finally reversed a string of declines in the preceding three quarters—the inflation-adjusted net export deficit deteriorated by almost $8 billion in the fourth quarter compared with the third. If the U.S. net export position had remained unchanged, U.S. GNP growth in the final quarter of 1985 would have been equal to the flash estimate—3.2 percent.

. . . As The Expansion Enters Its Fourth Year

The U.S. economy should experience a better performance this year than it did in 1985 and the drop in oil prices enhances this outlook. This improvement will be no small accomplishment in view of the fact that we have now completed 38 months of business expansion, and only two of the previous postwar peacetime recoveries lasted longer. The GNP after adjusting for inflation, is expected to increase at least 3½-percent this year compared with only 2-1/3 percent in 1985. The growth should be better balanced, with the goods-producing sector making more of a contribution this year than last, when services provided most of the thrust.

Consumer spending will continue to bolster the expansion. The record level of employment—both in terms of the number of people at work as well as when compared with the over-16 population—will provide consumers with good-sized gains in income and consequently with increased buying power. The rallies in both the stock and bond markets over the past three months have substantially increased the value of investors' assets—not to mention consumers' confidence—allowing people to continue a high rate of spending.

The outlook for business capital spending is less bright. Capacity utilization rates nationwide still stands at 80.5 percent—about five full percentage points below the level usually prevailing at this stage of the business cycle. The capital spending outlook is also clouded by the uncertainty associated with proposed tax reform legislation. As a result, business capital spending will be lackluster this year until the tax situation is clarified.

Another major factor in the acceleration of GNP growth will be the gradual improvement in the U.S.

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[illegible] expert [illegible] year [illegible] a [illegible] $46 [illegible]

Although [illegible]

rule of thumb is that every one-dollar drop in the price of a barrel of crude oil results in a two-cent decline in the price of a gallon of gasoline or of home heating oil. This implies that at $20 per barrel for oil, gasoline prices at the pump would fall about 16 cents a gallon. Lower oil prices should also mean [illegible] in the rates paid by utility users. [illegible] gas and electricity account for about one-tenth of [illegible] monthly housing expenses, so their [illegible] considerable saving in [illegible] budgets.

[illegible] benefit [illegible] some more than others, [illegible] industry, for example, 25 percent of [illegible]. Petroleum products are also among the [illegible] in the chemical industry.

Selected Federal Reserve Data

[illegible]

Reserve Bank Credit	Week Ending 1/29/86	[illegible]	[illegible]
U.S. Gov'ts and Agencies Owned Outright & RPs	[illegible]	2,311	+26,310
Loans to Depository Inst.	[illegible]	127	326
Float	[illegible]	+ 666	− 111
Total Reserve Bank Credit	[illegible]	674	+26,473
Treasury Deposits with Federal Reserve Banks	[illegible]	− 3,641	+12,541
Currency in Circulation	[illegible]	1,519	+13,588
Gov'ts held for Foreign Acct. by F.R. Banks (End of Week)	[illegible]	− 1,329	+10,680
Member Bank Reserves	1/29/86		
Total Reserves Held	[illegible]	2,955	+ 5,290
Excess (Deficiency)	[illegible]	802	+ 021
Net Free Reserves	[illegible]	782	+ 343
Monetary Aggregates †			
M1 (1/20/86)	[illegible]	+ 9.3	+ 11.34
M2 (December '85)	[illegible]	+ 5.5	+ 8.3
M3 (December '85)	[illegible]	+ 5.6	+ 7.2
Domestic Nonfinancial Debt (3rd Q'85)	[illegible]	+ 11.7	+ 13.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ [illegible]

New York Money Market

Offering Rates 1/31/86	[illegible]	[illegible]	1 Year
‡U.S. Treasury Bills	6.90%	7.00%	7.04%
*Federal Agencies	7.25	7.30	7.25
*Municipal Notes–High Grade (46% Taxable Equivalent)	9.26	9.44	9.72
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
*Secondary Market–Prime	7.74	7.75	7.80

‡Finance Company Paper–Prime		‡* Bankers' Acceptances	
5- 14 days	7.70%	Mar.	7.70%
15- 29 days	7.75	Apr.	7.65
30- 59 days	7.70	May	7.60
60- 89 days	7.65	Jun.	7.55
90-179 days	7.55	Jul.	7.55
180-239 days	7.50	Aug.	7.50
240-270 days	7.50		

‡Industrial Paper–Prime			
30- 89 days	7.65%	†Federal Funds Effective Rate	8.05%
90-120 days	7.45		

‡ [illegible] basis * [illegible] availability † Estimated

Selected Business Indicators

(All Dollar Figures in [illegible])

	[illegible]		[illegible]	Year Ago Period
Gross National Product (Current Dollars)*	[illegible]	$ 4,0[illegible]	$ 4,017	$ 3,853
Gross National Product (1982 Dollars)*	[illegible]	$ 3,[illegible]	$ 3,584	$ 3,516
Percent Change, Annual Rate	[illegible]	[illegible]	3.0	0.6
Change in Consumer Prices*	Dec. [illegible]	[illegible]	7.2%	3.6%
Change in Producer Prices*	Dec. [illegible]	[illegible]	9.6%	0.0%
Civilian Employment (Thousands of Persons) †	Dec. [illegible]	[illegible]	107,969	106,248
Unemployment as % of Civilian Labor Force †	Dec. [illegible]	[illegible]	7.0%	7.2%
Personal Income*	Dec. [illegible]	$ [illegible]	$ 3,347r	$ 3,207
Leading Indicators Composite Index (1967=100)†	Dec. [illegible]	[illegible]	172.0r	164.1
Industrial Production Index (1977=100) †	Dec. [illegible]	[illegible]	125.1	123.3
Net Change in Consumer Installment Credit †	Nov. [illegible]	$ [illegible]	$ 8.13	$ 6.08
U.S. Merchandise Trade Balance †	Dec. [illegible]	$ [illegible]	$ 13.68	$ 8.03
Plant and Equipment Expenditures*	[illegible]	$[illegible](a)	$388.98(a)	$371.16
Private Housing Starts (Thousands of Units)*	Dec. [illegible]	1,840	1,566	1,630
New Construction Expenditures*	Nov. 85	$ 348.2	$ 346.3	$ 313.1
Total Business Inventories †	Nov. 85	$ 583.4	$ 582.2	$ 571.2
Total Business Sales †	Nov. 85	$ 432.3	$ 426.0	$ 417.6

*Seasonally adjusted annual rate. †Seasonally adjusted. [illegible] Newly reported figure. r Revised. a Anticipated.

[illegible]

[illegible]

Conservation efforts adopted in this period will remain an important part of the energy picture. Efficiency improving and cost cutting practices still have high priority among industries and consumers. In addition, in the past dozen years, there has been a dramatic improvement in the fuel efficiency of the nation's car fleet. Undoubtedly, the strong increases in new car sales during the current expansion have accelerated the rise in fuel efficiency despite some renewed interest in larger cars. The average fuel efficiency of the U.S. car fleet is believed to have reached 17.2 miles per gallon in 1985, up from 13.1 in 1973.

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The next issue will be dated February 17.

Short Term [illegible] Outstandings

	[illegible]	[illegible]	[illegible]
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (1/15/86)	[illegible]	188	+8,886
New York City (1/22/86)	[illegible]	396	+2,165
Commercial Paper (1/22/86)	[illegible]	815	+58,181

Bank Loans

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (1/15/86)	[illegible]	– 696	+ 5,590
New York City (1/22/86)	[illegible]	– 272	– 2,229

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (1/15/86)	[illegible]	– 2,922	+ 71,050
New York City (1/22/86)	[illegible]	– 5,973	+ 16,965

Financial Markets

	Friday 1/31/86	Change from Week Ago	Change from Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	[illegible]	+ .02	[illegible] .91
180-Day Bills†	[illegible]	+ .03	.99
Longest Bills†	[illegible]	.12	1.39
Recent Issues:			
8⅛s 1/31/88	[illegible]	.17	
8⅜s 12/31/89	[illegible]	.18	
9⅛s 11/15/95	[illegible]	.14	
9⅞s 11/15/15	[illegible]	.11	
Municipals:			
Bond Buyer–20 Bond Index* (1/30/86)	[illegible]	.19	1.51
Blue List Total ($ Million)	[illegible]	+ $746	$ 286
30-Day Visible Supply ($ Million)	[illegible]	$967	$3,065
Total	[illegible]	$221	$3,351
Corporates:			
Moody's Aa Composite (1/30/86)	[illegible]	.06	1.85
30-Day Visible Supply ($ Million)	[illegible]	$440	+ $ 740
Stocks:			
Dow Jones Averages:			
Industrials	[illegible]	+ 41.06	+ 293.27
Transportation	[illegible]	+ 8.55	+ 138.52
Utilities	[illegible]	+ 5.70	+ 28.26
65 Stocks	[illegible]	+ 14.59	+ 115.47
N.Y.S.E. Composite Index	[illegible]	+ 2.81	+ 18.90
N.Y.S.E. Avg. Daily Vol. for Week (000's)	146,308	+25,494	+ 15,756

* 46% Taxable equivalent 14.56%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 1/31/86	Week Ago
Overnight	7.88%	7.69%
1 month	7.94	8.06
3 month	7.94	8.06
6 month	8.00	8.06
1 year	8.12	8.25
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	9.05%	9.20%
Long Term (7 to 15 yrs.)	9.60	9.65

FOREIGN EXCHANGE SPOT RATES

New York Opening (1/31/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02046	48.8800
Canada	.7021	1.4243
Denmark	.1141	8.7630
France	.1383	7.2308
Germany	.4186	2.3887
Italy	.0006142	1628.10
Japan	.005182	192.96
Mexico	.002235	447.50
Netherlands	.3705	2.6989
Switzerland	.4931	2.0279
U.K.	1.4130	.7077

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The Manufacturers Hanover Financial Digest

Economic Commentary,
Selected Financial Data,
and Business Indicators

FRIDAY, FEBRUARY 14, 1986

VOLUME XXIII, NUMBER 5

GNP Growth In 1986 Will Be Aided . . .

The Bureau of Labor Statistics' latest employment numbers provide a first glance at this year's economic prospects and, coming on the heels of several upbeat business statistics during the final months of last year, tend to confirm that the economy entered 1986 on a strong note. The number of people employed reached a record 109 million last month, while the number of people without jobs fell below the eight million mark for the first time since 1981. As a result, the unemployment rate retreated to 6.7 percent—the lowest rate in almost six years. While the service sector once again accounted for the bulk of the employment gain, it is encouraging that manufacturing employment increased for the fourth consecutive month, a trend which has reversed some 60 percent of the substantial decline in factory jobs which occurred between January and September of 1985.

Although the upturn in manufacturing employment is welcome in itself, even better news may be on the way. This is because the manufacturing sector should continue to improve throughout 1986 not only because of the weaker dollar in the foreign exchange markets but, perhaps equally important, because of the need to replenish inventories. The drag on growth stemming from both diminished inventory spending and a widening trade deficit may be about to end. Although December's monthly trade deficit surged to a record level, faster growth in Europe and the recent slide in the dollar—touching a seven-year low against the yen alone this week—suggest that the U.S. net export position should post a gradual improvement over the course of 1986. So, too, the contribution from inventory building is expected to increase.

. . . By Greater Inventory Accumulation . . .

The volatility in inventory spending and its effects on output can be seen in the economic growth rates posted over the past two years. Although inflation-adjusted GNP grew only 2.5 percent in 1985, substantially below the 6.6 percent rate of advance in 1984, the rate of growth in real final sales in both years did not differ substantially. Real final sales increased by four percent last year, compared with a 4.5 percent rise in 1984. The divergence in output in these years stemmed primarily from different postures toward inventory accumulation adopted by business.

Early in 1984, there was a feeling in the business community that inventories had gotten too low relative to current and projected sales. In addition, many businesses believed that the rate of inflation would accelerate as it typically does at this stage of the business cycle. That belief provided an incentive to stock up on goods since inflation would be increasing the value of goods on hand, thus boosting profitability. Furthermore, business plans for investment in plant and equipment were also strong, sending a signal to a wide variety of industries to gear up for the increased demands. As a result, inventory accumulation of almost $63 billion took place in 1984, contributing 2.1 percentage points to the real GNP growth rate.

On the other hand, this situation reversed itself last year. For one thing, retailers were shell-shocked from their experience during the 1984 holiday shopping season. They stocked up heavily in anticipation of strong holiday buying. Sales, however, fell short of expectations and retailers were caught with large amounts of unsold goods. They had to resort to substantial markdowns early in the holiday season to clear out surplus merchandise. For another, the low rate of inflation posted in 1984 combined with high real interest rates removed the incentive to stock up on merchandise. Businesses turned cautious, determined to keep their stocks as lean as possible. While this led to more efficient inventory management in 1985, the reduction in the rate of inventory accumulation restrained the growth in output.

The $7.3 billion increase in inflation-adjusted business inventories in 1985 marked a significant slowdown from the $62.6 billion accumulation pace of 1984. This deceleration depressed real GNP by more than $55 billion, subtracting 1.6 percentage points from last year's growth. If inventory spending last year had done no more than match the preceding year's rate, real GNP would have increased by 3.9 percent in 1985.

. . . As Industries Restock Their Shelves

It now seems that inventory building has slowed to the point where some snapback appears in the

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offing. The recently released monthly statistics on the manufacturing sector's inventories and shipments indicate that factory managers have not yet begun restocking their shelves. Inventories fell in December for the sixth straight month while shipments rose slightly. Out of the 14 major industries reporting, ten had inventories below their December 1984 levels. The biggest drop was in primary metals where inventories fell 14 percent over the year and were at their lowest point since April 1978. On the other hand, stock rebuilding was at its strongest in the transportation equipment sector.

For all manufacturing, the rise in shipments coupled with the drop in inventories pushed the inventory-sales ratio, which indicates how many months existing inventory would last if its was the only source for shipments, to its lowest level in two years. For individual industries, however, other factors—expected future prices of inputs, carrying costs and a product's shelf life—influence the optimum ratio of inventories to sales. In the food processing industry, for example, the short storage time of food dictates that inventories be kept consistently below the level of shipments. Even during the two recent recessions, the inventory-sales ratio never topped one month.

Another industry currently with a low ratio is the coal and petroleum sector. At .44, this industry had the lowest ratio of the industries reporting in December, an understandable development in light

Selected Federal Reserve Data

Averages of Daily Figures—Millions of Dollars

	Week Ending 2/12/86	Change From: Week Ago	Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies			
Owned Outright & RPs	180,484	−5,666	+15,136
Loans to Depository Inst.	596	−131	−499
Float	1,175	−301	+455
Total Reserve Bank Credit	198,105	−5,970	+18,555
Treasury Deposits with			
Federal Reserve Banks	6,854	−5,621	+2,057
Currency in Circulation	191,283	+668	+12,814
Gov'ts held for Foreign Acct. by F.R. Banks (End of Week)	128,231	−177	+12,005
	2/12/86		
Member Bank Reserves:			
Total Reserves Held	45,402	+194	+5,236
Excess (Deficiency)	1,186	+259	+174
Net Free Reserves	1,004	+451	+373
		% Change From: Three Months Ago*	Year Ago
Monetary Aggregates †			
M1 (2/3/86)	624.6	+10.1‡	+11.2‡
M2 (January '86)	2,567.1	+4.6	+7.0
M3 (January '86)	3,211.6	+6.1	+8.6
Domestic Nonfinancial Debt (3rd Q'85)	6,523.1	+11.7	+13.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four week moving average.

New York Money Market

Offering Rates 2/14/86	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	6.99%	7.08%	7.08%
* Federal Agencies	7.49	7.63	7.77
* Municipal Notes—High Grade (46% Taxable Equivalent)	9.07	9.44	9.44
Negotiable Time CDs: Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.67	7.70	7.75

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5-14 days	7.65%	Mar.	7.65%
15-29 days	7.70	Apr.	7.60
30-59 days	7.70	May	7.50
60-89 days	7.75	Jun.	7.45
90-179 days	7.65	Jul.	7.43
180-239 days	7.55	Aug.	7.38
240-270 days	7.45		

‡Industrial Paper—Prime			
30-89 days	7.75%	†Federal Funds	
90-120 days	7.65	Effective Rate	7.69%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	4th Q'85	$ 4,075	$ 4,017	$ 3,853
Gross National Product (1982 Dollars)*	4th Q'85	$ 3,605	$ 3,584	$ 3,516
Percent Change, Annual Rate	4th Q'85	2.4	3.0	0.6
Change in Consumer Prices*	Dec. '85	4.6%	7.2%	3.6%
Change in Producer Prices*	Jan. '86n	8.4%	6.0%r	−1.2%r
Civilian Employment (Thousands of Persons)†	Jan. '86n	108,966	108,206	106,315
Unemployment as % of Civilian Labor Force†	Jan. '86n	6.7%	6.9%	7.4%
Personal Income*	Dec. '85	$ 3,394	$ 3,347	$ 3,207
Leading Indicators Composite Index (1967=100)†	Dec. '85	173.6	172.0	164.1
Industrial Production Index (1977=100) †	Jan. '86n	126.1	126.3r	123.6
Net Change in Consumer Installment Credit †	Dec. '85n	$ [illegible]	$ 4.79r	$ 6.82
U.S. Merchandise Trade Balance †	Dec. '85	−$ 17.37	−$ 13.68	−$ 8.03
Plant and Equipment Expenditures*	1st Q'86	$402.13(a)	$388.98(a)	$371.16
Private Housing Starts (Thousands of Units)*	Dec. '85	1,840	1,566	1,630
New Construction Expenditures*	Dec. '85n	$ 354.6	$ 344.8r	$ 310.1
Total Business Inventories †	Dec. '85n	$ 582.2	$ 582.8r	$ 573.4
Total Business Sales †	Dec. '85n	$ 436.2	$ 432.0r	$ 421.6

*Seasonally adjusted annual rate. †Seasonally adjusted. n Newly reported figure. r Revised. a Anticipated.

of the price cuts that were taking place in the oil industry. Although shipments slowed, inventories deteriorated more sharply as firms shipped out more expensive crude in anticipation of replenishing stocks with cheaper, incoming oil.

Automakers also pushed inventories below the current monthly sales rate. Inventory rebuilding did begin last summer in the auto industry, but the jump in demand due to the August and September financing incentives cut into inventories and pushed down the inventory-sales ratio, although it remains high by Detroit's standards.

With inventories becoming a smaller source of available goods, production and employment has begun to turn around. After falling in eight of the first nine months of 1985, factory production employment has regained 164,000 jobs in the last four months. And the index of manufacturing production rose 1½ percent in November and December 1985. Unfortunately, while in the aggregate a move to replenish inventories will result in an increase in employment, the same is not true on an industry by industry basis since other factors influence labor decisions. For example, the chemical industry has increased inventories 11 percent since their recent trough in 1983, but improved production efficiency has boosted output thus eliminating many jobs.

The next issue will be dated March 3.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (1/29/86)	[illegible]	+ 627	+ 7,489
New York City (2/5/86)	[illegible]	+ 191	+ 3,562
Commercial Paper (2/5/86)	[illegible]	– 2,905	+ 51,395

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (1/29/86)	254,667	– 1,841	+ 3,999
New York City (2/5/86)	57,624	– 115	– 3,731

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (1/29/86)	717,134	– 3,359	+ 62,985
New York City (2/5/86)	155,631	+ 612	+ 14,141

Financial Markets

	Friday 2/14/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	[illegible]	21	– 1.22
180-Day Bills†	[illegible]	17	– 1.25
Longest Bills†	[illegible]	18	– 1.50
Recent Issues:			
8¹/₈s 1/31/88	[illegible]	18	
8³/₈s 12/31/89	[illegible]	33	
8⁷/₈s 2/15/96	[illegible]	– 43	
9¹/₄s 2/15/16	[illegible]	38	
Municipals:			
Bond Buyer–20 Bond Index* (2/13/86)	[illegible]	11	2.02
Blue List Total ($ Million)	$1,375	+ $ 63	– $ 422
30-Day Visible Supply ($ Million)	$ 680	+ $147	$2,158
Total	$2,055	+ $210	$2,579
Corporates:			
Moody's Aa Composite (2/13/86)	[illegible]	05	2.13
30-Day Visible Supply ($ Million)	$1,050	+ $125	+ $ 55
Stocks:			
Dow-Jones Averages:			
Industrials	[illegible]	+ 51.06	+ 382.43
Transportation	[illegible]	+ 10.56	+ 143.70
Utilities	[illegible]	+ 3.90	+ 29.80
65 Stocks	[illegible]	+ 16.45	+ 138.35
N.Y.S.E. Composite Index	[illegible]	+ 2.94	+ 21.38
N.Y.S.E. Avg. Daily Vol. for Week (000's)	140,110	9,048	+ 19,234

* 46% Taxable equivalent 14.11%

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 2/14/86	Week Ago
Overnight	7.69%	7.69%
1 month	7.88	7.88
3 month	7.88	8.00
6 month	7.94	8.00
1 year	8.06	8.25
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	8.80%	9.00%
Long Term (7 to 15 yrs.)	9.35	9.50

FOREIGN EXCHANGE SPOT RATES

New York Opening (2/14/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02074	48.21
Canada	.7171	1.3945
Denmark	.1153	8.6750
France	.1381	7.2425
Germany	.4239	2.3590
Italy	.0006221	1607.50
Japan	.005476	182.60
Mexico	.002151	465.00
Netherlands	.3753	2.6643
Switzerland	.5105	1.9590
U.K.	1.4180	.7052

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The Manufacturers
Hanover
Financial
Digest

Economic Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, MARCH 3, 1986

VOLUME XXIII, NUMBER 6

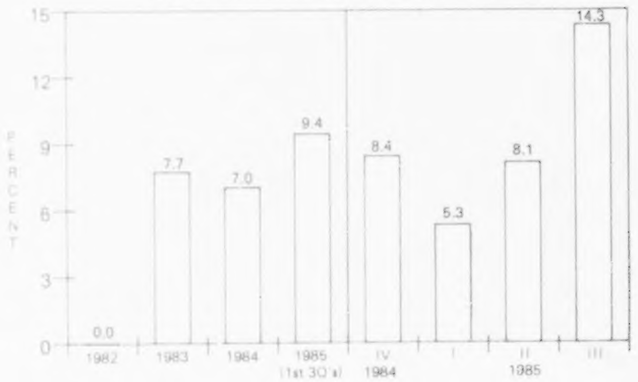
Monetary Policy . . .

Despite strong indications that today's monetary policy posture will remain essentially unchanged, and consequently that the Federal Reserve will not seek to aggressively push short-term interest rates lower, strong rallies persist in both the bond and stock markets. With oil prices slumping, prospects for lower inflation rates continue to send bond prices higher and yields in the opposite direction, while the likelihood of enhanced corporate profitability does the same for share prices. Not even the Congressional testimony of Fed Chairman Paul A. Volcker could dampen market enthusiasm for long; the markets took in stride the statements that no significant changes had recently been made in monetary policy and warnings of the potentially negative effects of too rapid a drop in the external value of the dollar. For while such comments may have dashed hopes of an imminent turn toward greater monetary ease, they don't preclude one forever—especially in light of the exceptionally good inflation rate outlook and the need of several high-debt, advanced developing countries for more interest rate relief.

One reason why the Fed may have decided to postpone further overt easing initiatives is the brightening business outlook. While there may be no boom on the horizon, there is certainly no bust, either. For one thing, recent trends in the index of leading economic indicators, payroll employment, housing starts and automobile sales all point to a strengthening pace of business. In January, payroll employment surged by more than 550,000, housing starts ran at their highest level in nearly two years, and automobile sales, stimulated by dealer financing incentives, ran at a better than nine million unit seasonally adjusted annual rate during the second ten-day selling period in February—one of the best levels since last autumn.

To be sure, such other signs as manufacturing employment, industrial production and nonauto retail sales do not paint quite as robust a picture. However, with domestic auto output running nearly ten percent ahead of the pace of last quarter, the trade deficit expected to narrow during the course of the year as a result of both the dollar's slide in the foreign exchange markets and a pickup in business activity in industrial Europe, and inventory spending poised to accelerate (Financial Digest—February 14, 1986), it appears a good bet that current business trends look good enough to preclude a quick turn toward ease.

FOREIGN INFLOWS AS A PERCENT OF
TOTAL FUNDS RAISED IN CREDIT MARKETS



. . . Should Be In A Holding Pattern . . .

So, too, recent Federal budget developments could be an obstacle to more ease. The Federal District Court decision that certain provisions of the Gramm-Rudman-Hollings Deficit Reduction Act are unconstitutional clearly set back Federal budget balancing efforts and, although the ruling will be appealed, the initial decision certainly clouds prospects that a credible deficit reduction program will be put in place any time soon. What is more, the release of the President's budget for fiscal year 1987 reinforces such uncertainty, promising little in the way of fiscal relief. For although a red-ink total of less than $144 billion is projected, it relies on a rather upbeat set of economic assumptions which may or may not come to pass.

More immediately, however, the Federal deficit should top $200 billion once again in the current fiscal year, despite the fact that nearly $12 billion of Gramm-Rudman mandated spending cuts are embodied in the current budget. As a result, while the Fed may eventually have to loosen the monetary

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rems if in fact Gramm-Rudman becomes law—and could have set the stage for the Fed [illegible] 1986 M1 growth target range [illegible] percent band by a [illegible] margin—the majority of [illegible] programs [illegible] however.

. . . In The Weeks Ahead

A[illegible] the President's [illegible] of the [illegible] Volcker [illegible]

rapid a dollar descent and its implications both for the financial markets as well as inflation expectations. For one thing, with foreign inflows recently accounting for about $1 of every $6 raised in the credit markets, a sharp tumble in the dollar's value, and a consequent loss of investor confidence in the currency, could hamper their smooth and efficient functioning and ultimately send interest rates [illegible]. For another, too rapid a fall of the dollar could lead to sharp boosts in import [illegible], offsetting to some extent the inflation [illegible] effects of lower energy prices. While it [illegible] the Fed [illegible] that too rapid a dollar [illegible] these concerns have to be kept in

Selected Federal Reserve Data

(Averages of Daily Figures—Millions of Dollars)

	Week Ending 2/26/86	$ Change From: Week Ago	$ Change From: Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies			
Owned Outright & RPs	[illegible]	– 601	+16,167
Loans to Depository Inst	[illegible]	– 123	– 316
Float	[illegible]	+ 113	496
Total Reserve Bank Credit	[illegible]	– 1,338	+18,488
Treasury Deposits with			
Federal Reserve Banks	[illegible]	+ 766	+ 2,884
Currency in Circulation	[illegible]	– 511	+13,067
Gov'ts held for Foreign Acct by F.R. Banks (End-of-Week)	[illegible]	1,863	–12,688
	2/26/86		
Member Bank Reserves			
Total Reserves Held	[illegible]	428	+ 5,325
Excess (Deficiency)	[illegible]	196	+ 191
Net Free Reserves	[illegible]	608	+ 168

		% Change From: Three Months Ago*	% Change From: Year Ago
Monetary Aggregates †			
M1 (2/17/86)	[illegible]	– 9.8‡	+ 11.0‡
M2 (January '86)	[illegible]	– 4.4	+ 6.9
M3 (January '86)	[illegible]	+ 8.0	+ 6.6
Domestic Nonfinancial Debt (3rd Q'85)	[illegible]	+ 11.7	+ 13.7

†Seasonally adjusted

* Seasonally adjusted annual rate

‡ Four-week moving average

New York Money Market

Offering Rates 2/28/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	6.99%	6.99%	6.91%
* Federal Agencies	7.20	7.10	7.00
* Municipal Notes—High Grade (46% Taxable Equivalent)	8.06	8.52	8.89
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.55	7.55	7.55

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5–14 days	7.55%	Mar.	7.65%
15–29 days	7.55	Apr.	7.60
30–59 days	7.60	May	7.50
60–89 days	7.55	Jun.	7.45
90–179 days	7.48	Jul.	7.35
180–239 days	7.35	Aug.	7.25
240–270 days	7.35		

‡ Industrial Paper—Prime			
30–89 days	7.53%	† Federal Funds Effective Rate	7.94%
90–120 days	7.40		

‡ Discount basis.   * Subject to availability.   † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period at End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	[illegible]	[illegible]	$ 4,017	$ 3,853
Gross National Product (1982 Dollars)*	[illegible]	[illegible]	$ 3,584	$ 3,516
Percent Change, Annual Rate	[illegible]	[illegible]	3.0	. 0.6
Change in Consumer Prices*	[illegible]	[illegible]	4.8%	2.4%
Change in Producer Prices*	[illegible]	[illegible]	6.0%	– 1.2%
Civilian Employment (Thousands of Persons) †	[illegible]	[illegible]	108,206	106,315
Unemployment as % of Civilian Labor Force †	[illegible]	[illegible]	6.9%	7.4%
Personal Income*	[illegible]	[illegible]	$ 3,386r	$3,217
Leading Indicators Composite Index (1967=100) †	[illegible]	[illegible]	172.0	164.1
Industrial Production Index (1977=100) †	[illegible]	[illegible]	126.3	123.6
Net Change in Consumer Installment Credit †	[illegible]	[illegible]	$ 4.79	$ 6.82
U.S. Merchandise Trade Balance †	[illegible]	[illegible]	–$ 15.15r	–$ 11.57r
Plant and Equipment Expenditures*	[illegible]	[illegible]	$388.98(a)	$371.16
Private Housing Starts (Thousands of Units)*	[illegible]	[illegible]	1,804r	1,804
New Construction Expenditures*	[illegible]	[illegible]	$ 344.8	$ 310.1
Total Business Inventories †	[illegible]	[illegible]	$ 582.8	$ 573.4
Total Business Sales †	[illegible]	[illegible]	$ 432.0	$ 421.6

*Seasonally adjusted annual rate   †Seasonally adjusted   [illegible]   r Revised.   a Anticipated.

mind. If easing the money reins prompted a significantly lower level of short-term interest rates, the downside vulnerability of the dollar would undoubtedly be increased, as would the potentially negative consequences (see chart on page 1).

What all this suggests [illegible] is that forces in the economy, the difficulties of the Gramm-Rudman budget-balancing bill, the [illegible] and fears of too-rapid a descent of the dollar in the foreign exchange markets tend to [illegible] against [illegible] easing of the monetary [illegible] at this time [illegible] other than the Fed [illegible] tightening [illegible] inflation rate pressures, still sizable chunks of unused capacity in the manufacturing sector and the ongoing external debt problems of the developing countries. What is more, if it tightened now and Federal spending is cut later as required by the Gramm-Rudman bill, the economy could be set on a dangerously recessionary course. With these assessments in mind, the Fed will postpone any new monetary policy initiatives, until such time as either the business or Federal budget outlooks change significantly. M

The next issue will be dated March 17.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (2/12/86)	[illegible]	– 480	– 8,692
New York City (2/19/86)	[illegible]	+ 67	+ 3,738
Commercial Paper (2/19/86)	[illegible]	+ 24	+50,809

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (2/12/86)	255,914	+ 92	+ 3,142
New York City (2/19/86)	57,983	+ 168	– 2,943

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (2/12/86)	715,878	– 4,294	+ 58,909
New York City (2/19/86)	159,188	+ 5,024	+ 18,167

Financial Markets

	Friday 2/28/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	[illegible]	0	– 1.60
180-Day Bills*	[illegible]	– .08	– 1.99
Longest Bills†	[illegible]	– .14	– 2.33
Recent Issues:			
8s 2/29/88	[illegible]	.23	
$8^3/8$s 12/31/89	[illegible]	.27	
$8^7/8$s 2/15/96	[illegible]	– .39	
$9^1/4$s 2/15/16	[illegible]	– .43	
Municipals:			
Bond Buyer—20 Bond Index* (2/27/86)	[illegible]	.46	– 2.73
Blue List Total ($ Million)	[illegible]	– $148	$ 509
30-Day Visible Supply ($ Million)	[illegible]	+ $368	$1,559
Total	[illegible]	+ $220	– $2,068
Corporates:			
Moody's Aa Composite (2/27/86)	[illegible]	– .42	3.10
30-Day Visible Supply ($ Million)	[illegible]	+ $799	$16
Stocks:			
Dow-Jones Averages:			
Industrials	1,709.06	+ 11.35	+ 409.70
Transportation	[illegible]	5.40	+ 156.98
Utilities	185.83	.30	+ 37.03
65 Stocks	674.83	+ 1.59	+ 151.50
N.Y.S.E. Composite Index	130.14	+ 1.33	+ 24.70
N.Y.S.E. Avg. Daily Vol. for Week (000's)	[illegible]	+ 7,762	+ 54,566

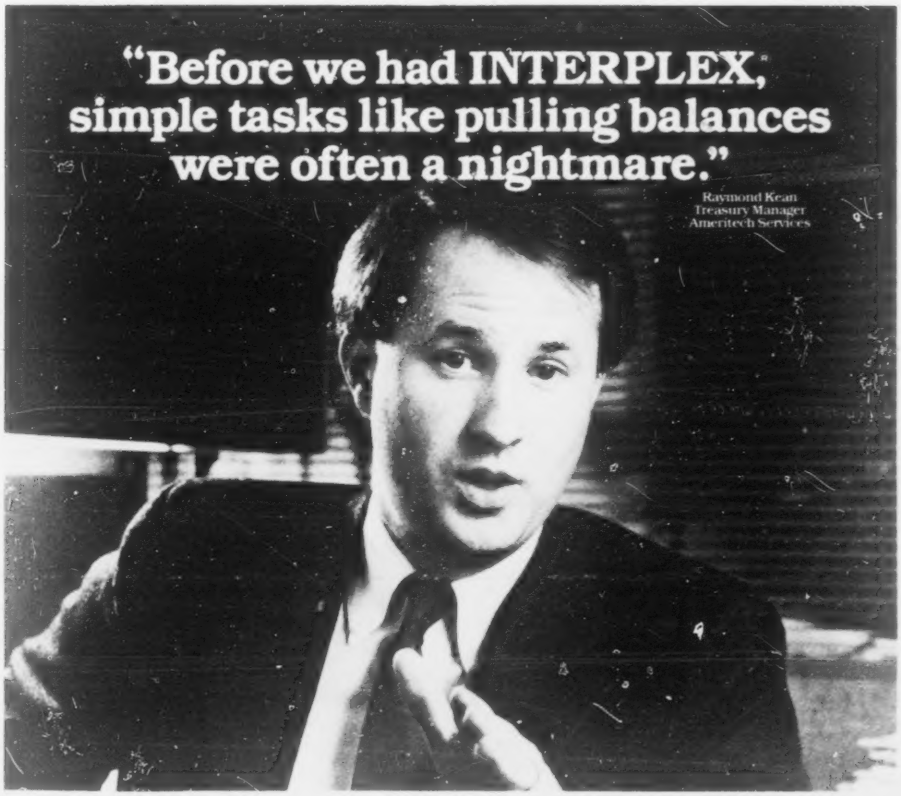
* 46% Taxable equivalent 12.93%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 2/28/86	Week Ago
Overnight	7.75%	7.81%
1 month	7.75	7.88
3 month	7.69	7.88
6 month	7.69	7.88
1 year	7.75	8.00
EURODOLLAR BONDS Average Yield		
Medium Term (5 to 7 yrs.)	8.50%	8.70%
Long Term (7 to 15 yrs.)	8.90	9.15

FOREIGN EXCHANGE SPOT RATES New York Opening (2/28/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02199	45.48
Canada	.7007	1.4272
Denmark	.1219	8.2050
France	.1466	6.8227
Germany	.4508	2.2185
Italy	.0006618	1511.00
Japan	.005556	179.99
Mexico	.002116	472.50
Netherlands	.3987	2.5079
Switzerland	.5340	1.8725
U.K.	1.4653	.6825



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The Manufacturers Hanover Financial Digest

Economic Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, MARCH 17, 1986

VOLUME XXIII, NUMBER 7

The Dollar Takes A Tumble . . .

Only one year ago, the dollar was invincible, soaring higher and higher in the foreign exchange markets at a breakneck pace, and shattering record levels almost daily against virtually every major currency. By mid-February of last year, it had climbed to 3.47 German marks, pierced the 10 French franc level, catapulted to over 2,200 lira and was rapidly approaching parity with the once-mighty British pound—to the chagrin of domestic exporters, but to the joy of tourists who flocked to Europe in record numbers for bargains. Since then, however, the dollar has experienced a rapid and virtually unprecedented decline, falling to its lowest level since November, 1981 against the mark, while flirting with its record low of 175.50 yen reached in October, 1978.

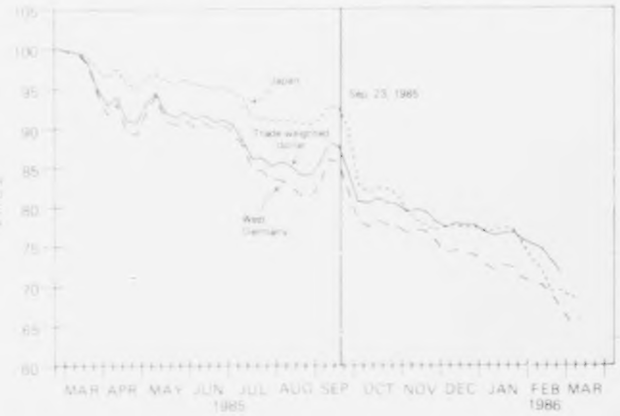
Perhaps the most important reason for the dollar's rapid descent has been a fundamental shift in the U.S. Administration's stance towards it. Whereas a year ago, Washington was championing the dollar's strength as an indication of market confidence in the vitality and dynamism of the U.S. economy, the Administration now has adopted a policy of talking down the dollar. Such a change was precipitated by the ballooning merchandise trade deficit—which last year reached a record $145 billion, or four times the size of the red-ink total of $36 billion posted at the beginning of this decade.

With domestic manufacturers finding themselves increasingly unable to compete effectively with imports, as well as unable to export, the Administration began to give high priority to reducing the dollar's value in order to stimulate exports and halt the rising tide of protectionist sentiment in Congress. One result, initiated by Treasury Secretary James Baker, was last September's Group of Five (G-5) meeting in which France, Germany, Great Britain, Japan, and the U.S. pledged to reduce the value of the dollar. Despite initial skepticism in the foreign exchange markets, the results of that meeting have gone beyond expectations. Paced by a 26 percent drop against the yen, and a 23 percent decline against the Deutschemark, the trade-weighted dollar has tumbled by some 18 percent since mid-September alone—and now stands nearly 30 percent below its February 1985 high (see chart).

. . . But It's No Panacea . . .

With that accomplished, the question now becomes whether or not the decline in the dollar will help to narrow the yawning trade gap. Unfortunately, the answer is not all that clear-cut. For the dollar's drop may not be the panacea that many in the Administration hope it will be. In this regard, recent comments by Federal Reserve Chairman Paul A. Volcker stressing the need for faster growth overseas are extremely relevant. It was rapid U.S. economic growth in 1983-1984, along with the rise in the value of the dollar, which laid the seeds for the present imbalance in our trade position, particularly as growth in many of our major markets was sluggish during this period. Exports, in fact, peaked in 1981 at $234 billion, and four years later were still nearly nine percent below that level. It is no coincidence that this period has been marked by extremely sluggish growth overseas.

U.S. DOLLAR DEPRECIATION VS. SELECTED CURRENCIES
(WEEK ENDING FEBRUARY 27, 1985 = 100)



Germany's economy, for instance, expanded by a paltry annual average of 1.2 percent between 1981 and 1985, while France's increase was at a similar pace and Italy crawled along at an annual average rate of less than one percent. Meanwhile, a good chunk of Latin America and many other developing nations saw their growth halted by weak commodity prices, increased servicing costs on their external debt, and rising protectionism in industrial country markets.

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There are, however, some reasons for cautious optimism about European growth prospects as a result of the steep fall in oil prices, the decline of the dollar and falling interest rates. Inflationary pressures have been muted, with price stability likely in Germany, the Netherlands and Switzerland while inflation rates in France, Austria, Belgium and Denmark should fall below three percent by yearend. Low inflation will boost real purchasing power, thus spurring consumer spending. Germany should lead European growth this year, a prospect made even more likely as a result of the German central bank's recent, one-half percentage point reduction in its discount rate—while growth in the the U.K. and France should pick up as well.

However, by the standards of the 1960s and early 1970s, the pace of business is likely to remain rather tepid, as double-digit rates of unemployment constrain activity levels throughout much of industrial Europe.

. . . For The Trade Deficit

While this could boost U.S. export prospects in Europe, among the Organization of Petroleum Exporting Countries (OPEC) and Latin America, in contrast, they remain decidedly weak. This is because of soft commodity prices and austerity policies designed to curb inflation. During the 1970s and early 1980s, these countries were particularly lucrative markets for U.S. exporters.

Selected Federal Reserve Data

(Averages of Daily Figures—Millions of Dollars)

	Week Ending 3/12/86	Change from Week Ago	Change from Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	[illegible]	307	+15,822
Loans to Depository Inst.	754	+ 100	− 1,284
Float	[illegible]	+ 404	+ 277
Total Reserve Bank Credit	200,181	+ 488	+18,864
Treasury Deposits with Federal Reserve Banks	[illegible]	981	− 565
Currency in Circulation	[illegible]	+ 1,110	+13,002
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	[illegible]	+ 606	+15,841
	3/12/86		
Member Bank Reserves			
Total Reserves Held	45,731	+ 776	+ 5,654
Excess (Deficiency)	909	− 127	+ 127
Net Free Reserves	[illegible]	+ 238	+ 539

		Change from Three Months Ago*	Change from Year Ago
Monetary Aggregates†			
M1 (3/3/86)	631.8	+ 8.1‡	+ 10.8‡
M2 (February '86)	2,577.0	+ 4.1	+ 6.4
M3 (February '86)	3,739.8	+ 7.3	+ 6.8
Domestic Nonfinancial Debt (4th Q'85)	6,867.9	+ 19.2	+ 14.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 3/14/86	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	6.76%	6.90%	6.97%
* Federal Agencies	6.73	6.74	6.72
* Municipal Notes—High Grade (46% Taxable Equivalent)	7.78	8.06	8.33
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.15	7.15	7.15

‡Finance Company Paper—Prime	
5–14 days	7.20%
15–29 days	7.20
30–59 days	7.15
60–89 days	7.10
90–179 days	7.05
180–239 days	7.00
240–270 days	7.00

‡* Bankers' Acceptances	
Mar.	7.20%
Apr.	7.15
May	7.05
Jun.	7.00
Jul.	6.97
Aug.	6.93

‡Industrial Paper—Prime	
30–89 days	7.05%
90–120 days	8.50

†Federal Funds Effective Rate 7.28%

‡Discount rates. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period in	End of Period	Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	4th Q'85	$ 4,0[illegible]	$ 4,017	$ 3,853
Gross National Product (1982 Dollars)*	4th Q'85	$ 3,5[illegible]	$ 3,584	$ 3,516
Percent Change, Annual Rate	4th Q'85	1.2	3.0	0.6
Change in Consumer Prices*	Jan. '86	2.[illegible]%	4.8%	2.4%
Change in Producer Prices*	Feb. '86p	−19.2%	− 8.4%	0.0%
Civilian Employment (Thousands of Persons)†	Feb. '86p	108,561	108,955	106,587
Unemployment as % of Civilian Labor Force†	Feb. '86p	7.3%	6.7%	7.3%
Personal Income*	Jan. '86	$ 3,[illegible]	$ 3,386	$3,217
Leading Indicators Composite Index (1967=100)†	Jan. '86p	173.0	174.0r	166.3
Industrial Production Index (1977=100) †	Feb. '86p	125.1	126.5	123.7
Net Change in Consumer Installment Credit †	Jan. '86p	$ 6.88	$ 5.62r	$ 7.22
U.S. Merchandise Trade Balance †	Jan. '86	−$ 16.46	−$ 15.15	−$ 11.57
Plant and Equipment Expenditures*	1st Q'86	$402.13(a)	$388.98(a)	$371.16
Private Housing Starts (Thousands of Units)*	Jan. '86	2,088	1,804	1,804
New Construction Expenditures*	Jan. '86p	$ 357.[illegible]	$ 354.0r	$ 341.0
Total Business Inventories †	Jan. '86p	$ 588.1	$ 584.0r	$ 575.0
Total Business Sales †	Jan. '86p	$ 433.5	$ 435.0r	$ 417.4

*Seasonally adjusted annual rate. †Seasonally adjusted. p Newly reported figure. r Revised. a Anticipated.

Whereas exports to Mexico, for example, averaged nearly $15 billion annually during the 1980-82 period, they have since slumped, averaging just $11½ billion annually during the three years since then. To be sure, while other industrial nations face a similar problem, none are as dependent upon these markets as the U.S. is. Further hindering export prospects are continued weak grain prices as a result of the worldwide grain glut. Last year, 14 percent of all U.S. exports were grain.

Thus, the decline in the dollar alone will be no panacea. It should, of course, help to stabilize the trade deficit, but the red ink totals will remain sizable. In this regard, falling oil prices and somewhat faster growth in Europe are to be welcomed. But a much more favorable global economic environment is necessary in order to significantly narrow the trade deficit, forestall a rise in protectionist sentiment, and enable U.S. exporters to take full advantage of the decline of the dollar. At a minimum, such an environment requires a pronounced pickup in world trade growth and a stepped-up flow of financial resources to the high-debt, advanced developing countries. Hopefully, the seeds for such growth were sown earlier this month in the coordinated reduction of central bank discount rates by several major industrial nations—the harvest from which may become apparent later this year.

Short Term Paper Outstanding
(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (2/26/86)	[illegible]	+ 138	– 1,406
New York City (3/5/86)	[illegible]	– 267	– 3,096
Commercial Paper (3/5/86)	[illegible]	+ 111	+48,813

Bank Loans
(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (2/26/86)	257,749	+ 1,170	+ 4,493
New York City (3/5/86)	58,951	+ 586	– 3,380

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (2/26/86)	722,473	– 2,896	+ 63,988
New York City (3/5/86)	164,010	+ 7,088	+ 20,529

Financial Markets

	Friday 3/14/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	[illegible]	.04	– 1.96
180-Day Bills†	[illegible]	– .06	– 2.61
Longest Bills†	[illegible]	– .12	– 3.00
Recent Issues:			
8s 2/29/88	[illegible]	– .15	
8³/₈s 12/31/89	[illegible]	– .18	
8⁷/₈s 2/15/96	[illegible]	– .30	
9¹/₄s 2/15/16	[illegible]	– .26	
Municipals:			
Bond Buyer—20 Bond Index* (3/13/86)	[illegible]	+ .01	– 2.87
Blue List Total ($ Million)	[illegible]	+$ 281	+ $ 53
30-Day Visible Supply ($ Million)	[illegible]	+$ 984	– $ 642
Total	[illegible]	+$1,265	– $ 589
Corporates:			
Moody's Aa Composite (3/13/86)	[illegible]	.13	– 3.48
30-Day Visible Supply ($ Million)	[illegible]	+$1,565	+ $2,520
Stocks:			
Dow Jones Averages:			
Industrials	[illegible]	+ 93.11	+ 545.92
Transportation	[illegible]	+ 24.90	+ 214.05
Utilities	[illegible]	+ 7.64	+ 42.47
65 Stocks	[illegible]	+ 31.47	+ 199.31
N.Y.S.E. Composite Index	[illegible]	+ 5.79	+ 33.71
N.Y.S.E. Avg. Daily Vol. for Week (000's)	[illegible]	+17,726	+ 78,982

* 46% Taxable equivalent 12.76%.

† Bond equivalent

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 3/14/86	Week Ago
Overnight	7.31%	7.38%
1 month	7.50	7.50
3 month	7.38	7.44
6 month	7.38	7.44
1 year	7.38	7.44

EURODOLLAR BONDS Average Yield	Friday 3/14/86	Week Ago
Medium Term (5 to 7 yrs.)	8.08%	8.40%
Long Term (7 to 15 yrs.)	8.58	8.80

FOREIGN EXCHANGE SPOT RATES New York Opening (3/14/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02162	46.25
Canada	.7164	1.3958
Denmark	.1181	8.4675
France	.1439	6.9513
Germany	.4426	2.2595
Italy	.0006470	1538.50
Japan	.005666	176.50
Mexico	.002130	469.50
Netherlands	.3920	2.5513
Switzerland	.5272	1.8968
U.K.	1.4668	.6818

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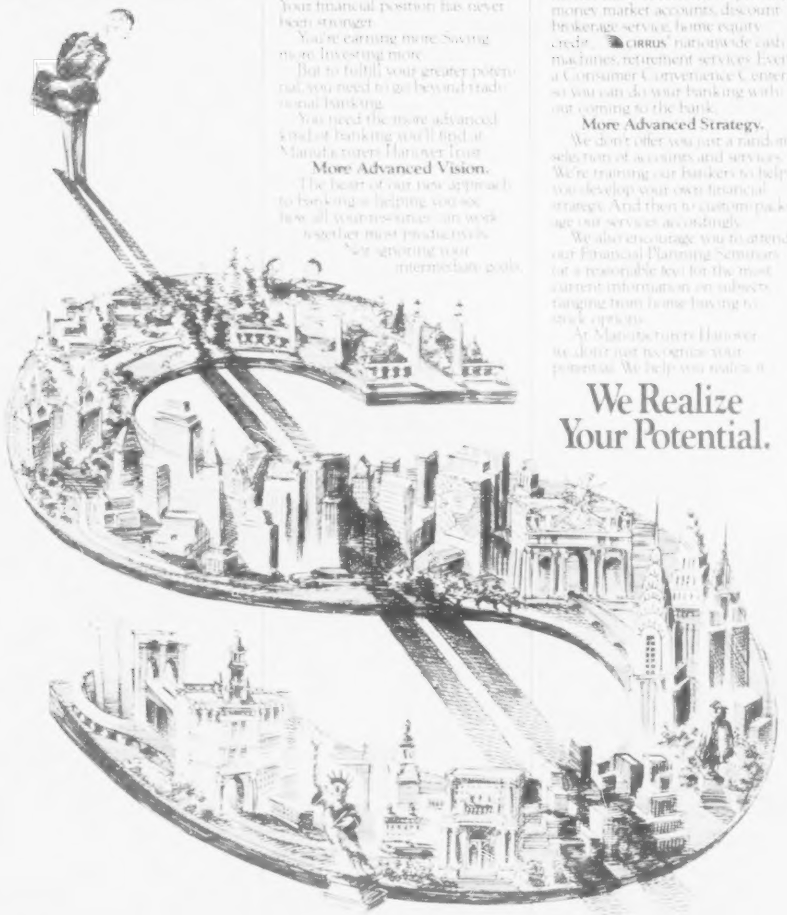

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The Manufacturers Hanover Financial Digest

Economic Commentary,
Selected Financial Data,
and Business Indicators

FRIDAY, MARCH 28, 1986

VOLUME XXIII, NUMBER 8

The Big Apple's Job Growth . . .

New York City's economy prospered in 1985 along with the U.S. economy. With 3.5 million jobs, the City's employment was at its highest level since 1973. A total of 51,000 new jobs was added to payrolls last year on the heels of a record 79,000 new positions created in 1984. Not since 1969 did the City generate employment gains of more than 50,000 a year for two consecutive years. Last year's employment gains, however, were again confined to nonmanufacturing industries. The shakeout in manufacturing employment continued, as more than 22,000 factory jobs were lost during the year.

In the private nonmanufacturing sector, employment gains were posted across a broad spectrum of industries. Paced by strong gains in business and legal services, the service sector—the largest single source of employment in the City—added 32,600 new jobs to its payrolls. As a result, the job count in that sector climbed to an all-time high of over 1,038,000 in 1985. The trade sector increased its employment by 11,200 positions, while construction hired 10,700 workers. Although construction contributed only one of every five new jobs created last year, it was the leading industry in the City in terms of its rate of growth. Construction employment surged 11.3 percent last year from its 1984 level. By comparison, employment in the service sector, which contributed two of every three new jobs created last year, increased by only 3.2 percent. Growth in construction employment nationwide, rising by only 7.3 percent, also did not match New York City's performance.

. . . Is Paced By Services . . .

After a glimmer of hope in 1984, when the factory job count dipped by only 3,000 compared with an average of 20,000 factory jobs lost annually in the five preceding years, manufacturing employment resumed its plunge in 1985. More than 22,000 factory jobs were lost last year, representing an erosion of 5.2 percent of the City's 1984 manufacturing base. Thus, the transition toward a service-based economy in New York City is clearly continuing, and the work force is increasingly being dominated by white-collar positions.

Since 1977, when the City's economic resurgence from the painful fiscal crisis of the mid-1970s began, New York City has gained almost 430,000 nonmanufacturing jobs while manufacturing employment has shrunk by more than 131,000 positions—a decline of 24.4 percent. In other words, one in every four factory jobs in the City disappeared in less than a decade. As a result of these declines, manufacturing employment in New York City averaged only 407,000 in 1985, the lowest level in the postwar period. In comparison, in 1950 the City's factories employed more than a million people.

Nationally, manufacturing employment rebounded in 1984 with an increase of over five percent, and inched up another 0.1 percent last year. The problems of the manufacturing sector nationwide are often attributed to the decline of mature, smokestack-type durable goods industries. Such industries, however, account for a very small percentage of factory jobs in the City. The City's manufacturing base is dominated by nondurable manufacturing which employs nearly three of every four factory workers.

It would appear that the main reason for the City's manufacturing decline is a continuing deterioration in its competitive position as a site for this type of activity. For example, the American apparel industry has suffered from severe foreign competition in recent years. However, losses in that industry's employment in New York City—it is the largest manufacturing employer—were much greater than nationally. Printing and publishing—the second largest manufacturing industry in the City—has been one of the fastest growing manufacturing sectors nationally. In the last four years, its employment expanded by more than 12 percent. In New York City, however, printing and publishing payrolls shrunk by three percent in the same period.

. . . While Manufacturing Declines

The composition of the City's employment growth has changed in recent years. Between 1978 and 1982, banking, finance, insurance and real estate and other services provided the strongest increase in new job creation, but this is no longer true. The banking sector, for example, hired an average of

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about 9,000 people annually between 1979 and 1982, in the past three years, however, New York City banks reduced their payrolls by almost 4,000 positions. On the other hand, employment in retail and wholesale trade which had shrunk almost 20 percent between 1963 and 1983, rebounded with an increase of more than 20,000 new jobs in 1984 and another 11,200 in 1985. At the same time, all levels of government began adding to their payrolls as the City's and the State's financial difficulties eased. Government employment increased by more than 30,000 in the last two years, a gain not seen since the 1960s.

The City's increasing prosperity is no longer limited to Manhattan. Although much of the post-1977 employment growth has been centered primarily in Manhattan, by 1984 other boroughs began to reap benefits from a strong resurgence of the City's economy as well. In the past two years, employment increased in all five boroughs. However, whereas in 1984 Manhattan accounted for more than half of all employment gains city-wide, in the first half of 1985 job growth in the boroughs outside Manhattan contributed two-thirds of the City's job increase. It was the first time since 1965 that the employment growth of the other boroughs exceeded Manhattan's.

The turnaround was most noticeable in Queens.

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 3/12/86	$ Change From: Week Ago	$ Change From: Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	183.309	– .307	+15.822
Loans to Depository Inst.	.754	+ .100	– 1.284
Float	.783	+ .404	+ .277
Total Reserve Bank Credit	200.181	+ .488	+18.864
Treasury Deposits with Federal Reserve Banks	3.496	– .981	– .565
Currency in Circulation	192.432	+ 1.110	+13.002
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	133.307	+ .606	+15.841
	3/12/86		
Member Bank Reserves:			
Total Reserves Held	45.731	+ .776	+ 5.654
Excess (Deficiency)	.909	– .127	+ .127
Net Free Reserves	.680	+ .238	+ .539

		% Change From: 3 Months Ago*	% Change From: Year Ago*
Monetary Aggregates †			
M1 (3/17/86)	638.4	+ 7.1‡	+ 11.2‡
M2 (February '86)	2,577.0	+ 4.1	+ 6.4
M3 (February '86)	3,239.8	+ 7.3	+ 6.8
Domestic Nonfinancial Debt (4th Q'85)	6,867.9	+ 19.2	+ 14.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 3/27/86	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	6.36%	6.34%	6.39%
* Federal Agencies	6.70	6.58	6.56
* Municipal Notes—High Grade (46% Taxable Equivalent)	7.59	7.69	8.33
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	7.14	7.10	7.10

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	7.25%	Apr.	7.20%
15- 29 days	7.25	May	7.10
30- 59 days	7.25	Jun.	7.00
60- 89 days	7.20	Jul.	6.95
90-179 days	7.12	Aug.	6.90
180-239 days	6.90	Sep.	6.80
240-270 days	6.90		

‡Industrial Paper—Prime			
30- 89 days	7.25%	†Federal Funds	
90-120 days	7.15	Effective Rate	7.40%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period	Data Reported	Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	4th Q'85	$ 4,059r	$ 4,017	$ 3,853
Gross National Product (1982 Dollars)*	4th Q'85	$ 3,591r	$ 3,584	$ 3,516
Percent Change, Annual Rate	4th Q'85	0.7r	3.0	0.6
Change in Consumer Prices*	Feb '86n	4.8%	3.6%	3.6%
Change in Producer Prices*	Feb '86	19.2%	– 8.4%	0.0%
Civilian Employment (Thousands of Persons) †	Feb '86	108,561	108,955	106,587
Unemployment as % of Civilian Labor Force †	Feb '86	7.3%	6.7%	7.3%
Personal Income*	Feb '86n	$ 3,406	$ 3,387r	$ 3,247
Leading Indicators Composite Index (1967=100) †	Jan '86	173.0	174.0	166.3
Industrial Production Index (1977=100) †	Feb '86	125.7	126.5	123.7
Net Change in Consumer Installment Credit †	Jan '86	$ 6.88	$ 5.62	$ 7.22
U.S. Merchandise Trade Balance †	Feb '86n	$ 12.49	–$ 14.42r	–$ 11.45
Plant and Equipment Expenditures*	1st Q'86	$402.13(a)	$388.98(a)	$371.16
Private Housing Starts (Thousands of Units)*	Feb '86n	1,985	2,056r	1,632
New Construction Expenditures*	Jan '86	$ 357.3	$ 354.0	$ 341.0
Total Business Inventories †	Jan '86	$ 588.1	$ 584.0	$ 575.0
Total Business Sales †	Jan '86	$ 433.5	$ 435.0	$ 417.4

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

Paced by strong increases in services, trade and construction, the borough's employment increased by almost 11,000 between January and June 1985, surpassing an increase of only 10,000 new positions in Manhattan.

As every commuter knows, New York City draws its labor force from the entire metropolitan region encompassing 22 counties of New York, New Jersey and Connecticut. However, New York City residents benefited from the improved opportunities in the last two years to a greater extent than in prior years when the bulk of new jobs was filled by non-residents. Almost 200,000 of City residents entered the ranks of jobholders in the last two years, whereas in the two preceding years, the number of residents working declined by almost 76,000. In fact, last year, the number of employed City residents hit the highest level in a decade, as a record 163,000 residents found new jobs. Consequently, the City's jobless rate fell to 8,1 percent of the labor force in 1985 from 8.9 percent a year earlier. It remained, however, well above the 7.2 percent average unemployment rate for the country as a whole and 6.5 percent of the jobless rate in New York State. Although the number of unemployed New Yorkers declined 13,000 in 1985 from the previous year, 265,000 residents of the City were still unable to find employment in 1985.

Short Term Paper Outstanding

Millions of Dollars

	Latest Week	Change Since Week Ago	Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (3/12/86)	162,799	– 263	+ 5,853
New York City (3/5/86)	36,708	– 267	+ 3,096
Commercial Paper (3/5/86)	297,456	+ 111	+48,813

Bank Loans

Millions of Dollars

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Year Ago
Nationwide (3/12/86)	258,794	– 794	+ 2,308
New York City (3/5/86)	58,951	+ 586	– 3,380

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Year Ago
Nationwide (3/12/86)	732,658	– 1,640	+ 68,667
New York City (3/5/86)	164,010	+ 7,088	+ 20,529

Financial Markets

	Thursday 3/27/86	Change Since Week Ago	Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.53%	– .06	– 1.92
180-Day Bills†	6.61	– .20	– 2.42
Longest Bills†	6.79	– .19	– 2.67
Recent Issues:			
8s 2/29/88	7.04	– .12	
8³/8s 12/31/89	7.18	– .17	
8⁷/8s 2/15/96	7.50	– .29	
9¹/4s 2/15/16	7.66	– .32	
Municipals:			
Bond Buyer–20 Bond Index* (3/26/86)	7.21%	– .13	– 2.54
Blue List Total ($ Million)	$1,718	–$ 130	+ $ 255
30-Day Visible Supply ($ Million)	$3,609	+$ 853	– $ 378
Total	$5,327	+$ 723	– $ 123
Corporates:			
Moody's Aa Composite (3/26/86)	9.46%	– .06	– 3.48
30-Day Visible Supply ($ Million)	$5,070	+$2,610	+ $4,595
Stocks:			
Dow-Jones Averages:			
Industrials	1,821.72	+ 17.48	+ 554.94
Transportation	828.39	+ 16.32	+ 225.31
Utilities	191.53	+ 6.88	+ 38.42
65 Stocks	717.13	+ 11.52	+ 202.02
N.Y.S.E. Composite Index	137.69	+ 1.56	+ 33.09
N.Y.S.E. Avg. Daily Vol. for Week (000's)	156,010	– 492	+ 62,694

* 46% Taxable equivalent 13.35%.

† Bond equivalent.

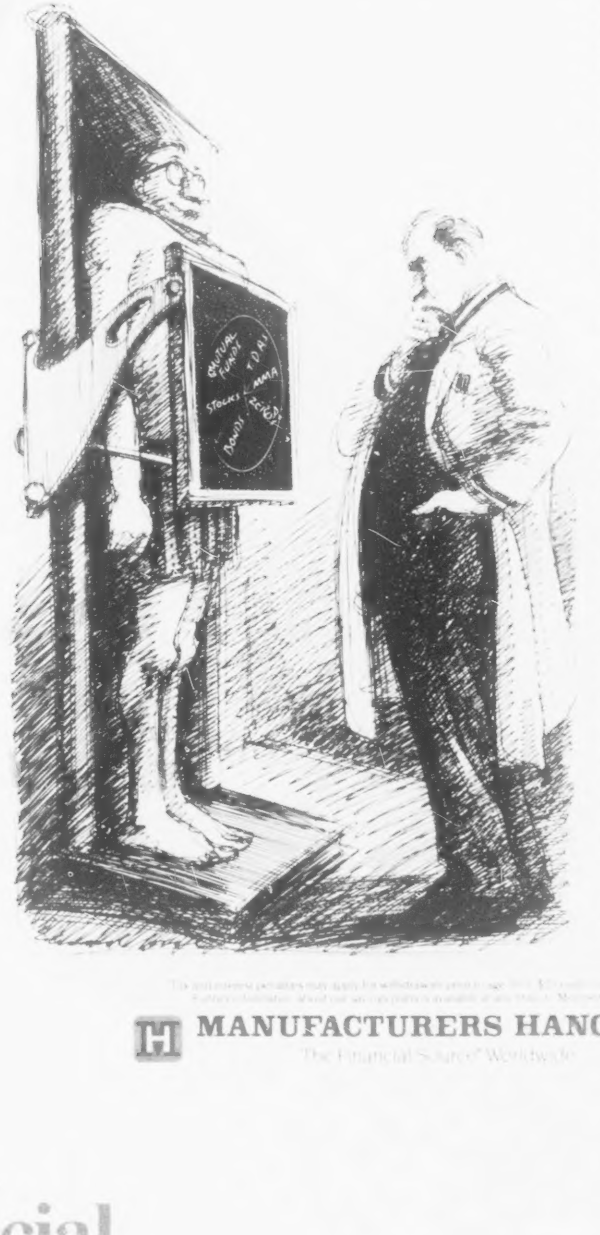
International Rates

	Thursday 3/27/86	Week Ago
EURODOLLAR DEPOSIT RATES (bid)		
Overnight	7.88%	7.13%
1 month	7.38	7.50
3 month	7.31	7.38
6 month	7.31	7.38
1 year	7.31	7.44
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.86%	7.98%
Long Term (7 to 15 yrs.)	8.30	8.59

FOREIGN EXCHANGE SPOT RATES

New York Opening (3/27/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02106	47.48
Canada	.7146	1.3993
Denmark	.1168	8.5600
France	.1403	7.1300
Germany	.4317	2.3163
Italy	.0006345	1576.00
Japan	.005574	179.42
Mexico	.002068	483.50
Netherlands	.3828	2.6120
Switzerland	.5156	1.9395
U.K.	.6732	1.4855

How healthy is your IRA?



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The Manufacturers Hanover Financial Digest

Economic Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, APRIL 14, 1986

VOLUME XXIII, NUMBER 9

The Economic Outlook In Europe . . .

After years of lackluster growth, lofty energy costs, slumping currencies and tight fiscal and monetary policies, the gauges of European economic health have brightened considerably in recent months. Better-coordinated economic policies have lowered inflation rates, improved trade performance, reduced budget deficits and allowed interest rates to fall. What is more, these policies have narrowed the differentials in economic performance among the strong and weak countries. Converging rates of growth, inflation and interest, in turn, have produced more exchange rate stability within the European Economic Community (E.E.C.) than has been seen in the past. Now, with these essential ingredients in place, Europe finds itself in a good position to exploit fully the growth opportunities offered by sharply falling oil prices and interest rates—good news for not only Europe's 19 million unemployed, but the global economy as well.

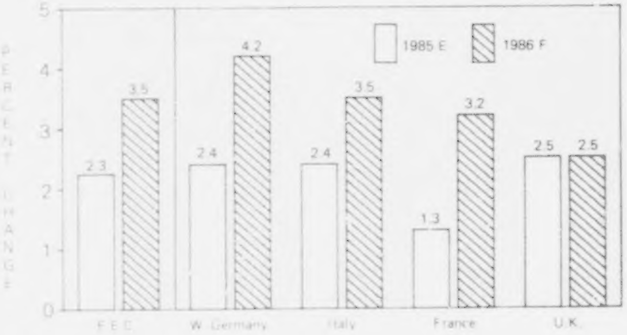
Reflecting the widespread reluctance to loosen fiscal policies for fear of reigniting inflation, Europe needed a spark to get itself back on the growth track. Substantially lower oil costs, magnified in terms of local currencies by the weaker external value of the dollar since oil is priced in dollars, should be that spark. If oil prices remain below $15 per barrel, for example, Western Europe could save nearly $50 billion on its imported oil bill this year, almost half the money spent on such purchases in 1985. By enhancing consumer purchasing power, the slide in energy costs will give Europe's private sector the equivalent of a tax cut without enlarging government budget deficits.

What is more, the dollar's descent over the past year will supplement the benefits of lower oil prices. Take, for example, Germany. The slide in dollar oil prices, combined with the nearly 30 percent appreciation of the Deutschemark relative to the dollar over the past year, have lowered the local currency cost of oil per barrel by some 70 percent. A similar case can be made for other oil-importing European countries whose currencies have recently appreciated against the dollar. In addition, because central banks no longer have to maintain high interest rates to support their currencies against a strong dollar, interest rates should fall further, fostering economic growth.

. . . Finally Begins To Brighten . . .

Although Europe's export competitiveness may be hurt by the drop in the dollar's value, the long-awaited pickup in domestic consumption and investment should more than offset any decline in the external stimulus. For one thing, falling oil prices and interest rates have sent European stock markets surging. The wealth effect of higher share prices, combined with lower inflation rates, should give a boost to consumer spending this year. For another, lower energy costs and the weaker dollar will decrease the costs of production, increasing industrial profitability—one of the necessary preconditions for more robust capital spending. According to recent surveys, European businesses intend to increase plant and equipment outlays by some ten percent this year after adjustment for inflation, versus about 1½ percent in the U.S. With domestic spending supplementing the export sector, growth throughout the E.E.C. could hit 3½ percent this year, or nearly double the average annual rate of rise posted during the immediately preceding three years (see chart).

REAL GNP GROWTH: TOTAL EUROPE AND SELECTED EUROPEAN COUNTRIES



Although opinion is divided as to whether Europe's expansion will outpace that of the U.S. in 1986, the continent's ability to share the role of locomotive for world growth can only have positive ramifications for the global economy. The worldwide economic

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recovery will be more sustainable if it does not depend upon the performance of any one country. Converging economic growth rates, moreover, will help alleviate some of the present imbalances and distortions in world trade.

A rebound in both European and world trade growth would be a welcome tonic for the global economy in general, and hard-pressed exporters in both Latin America and the United States in particular. Take, for example, Latin America. Whereas Latin American exports to Europe had been rising at hefty double-digit annual rates for several years prior to the onset of Europe's 1981-82 recession, they have since nosedived. By 1984, the value of such exports to the E.E.C. was still nearly six percent below its 1980 peak. What is more, whereas industrial Europe had been absorbing more than one fifth of Latin America's exports in the late 1970s, it currently takes in the neighborhood of one sixth.

. . . Boosting Global Business Prospects

Who picked up the slack? By and large, the United States, whose share of Latin American global exports rose from about 35 percent in the late 1970s to 45 percent in 1985. This suggests that any increase in European growth and expansion of its markets should not only enhance Latin American export earnings, but also reduce the vulnerability of such earnings to swings in U.S. economic performance.

Selected Federal Reserve Data

(Averages of Daily Figures—Millions of Dollars)

	Week Ending 4/9/86	$ Change From: Week Ago	$ Change From: Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies			
Owned Outright & RPs	184,947	+ .111	+14.434
Loans to Depository Inst.	952	+ .157	− .911
Float	691	− .375	− .122
Total Reserve Bank Credit	201,429	− .309	+16.808
Treasury Deposits with			
Federal Reserve Banks	3,365	+ .439	− .824
Currency in Circulation	194,369	+ 1,138	+13,055
Gov'ts held for Foreign Acct.			
by F.R. Banks (End-of-Week)	142,214	+ 2,216	+26,943
	4/9/86		
Member Bank Reserves:			
Total Reserves Held	46,695	+ 1,011	+ 5,895
Excess (Deficiency)	621	− .374	+ .064
Net Free Reserves	.323	− .438	+ .246

		% Change From: Three Months Ago	% Change From: Year Ago
Monetary Aggregates †			
M1 (3/31/86)	640.1	+ 8.0‡	+ 11.7‡
M2 (March '86)	2,589.9	+ 3.8	+ 6.6
M3 (March '86)	3,256.6	+ 7.2	+ 7.0
Domestic Nonfinancial Debt (4th Q'85)	6,867.9	+ 19.2	+ 14.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four week moving average.

New York Money Market

Offering Rates 4/11/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	6.17%	6.26%	6.30%
* Federal Agencies	6.42	6.47	6.59
* Municipal Notes—High Grade (46% Taxable Equivalent)	7.78	7.78	8.15
Negotiable Time CDs			
Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.52	6.52	6.50

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	6.65%	May	6.60%
15- 29 days	6.65	Jun.	6.40
30- 59 days	6.55	Jul.	6.40
60- 89 days	6.55	Aug.	6.35
90-179 days	6.45	Sep.	6.30
180-239 days	6.30	Oct.	6.25
240-270 days	6.30		

‡Industrial Paper—Prime		†Federal Funds	
30- 89 days	6.56%		
90-120 days	6.38	Effective Rate	6.78%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	[illegible]	[illegible]	Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	[illegible]	[illegible]	$ 4,017	$ 3,853
Gross National Product (1982 Dollars)*	[illegible]	[illegible]	$ 3,584	$ 3,516
Percent Change, Annual Rate	[illegible]	[illegible]	3.0	0.6
Change in Consumer Prices*	[illegible]	[illegible]	3.6%	3.6%
Change in Producer Prices*	[illegible]	[illegible]	− 19.2%	0.0%
Civilian Employment (Thousands of Persons)†	[illegible]	[illegible]	108,561	106,951
Unemployment as % of Civilian Labor Force†	[illegible]	[illegible]	7.3%	7.3%
Personal Income*	[illegible]	[illegible]	$ 3,387	$ 3,247
Leading Indicators Composite Index (1967=100)†	[illegible]	[illegible]	174.1r	167.4
Industrial Production Index (1977=100) †	[illegible]	[illegible]	126.5	123.7
Net Change in Consumer Installment Credit †	[illegible]	[illegible]	$ 5.62	$ 7.22
U.S. Merchandise Trade Balance †	[illegible]	[illegible]	−$ 14.42	−$ 11.45
Plant and Equipment Expenditures*	[illegible]	[illegible]	$388.98(a)	$371.16
Private Housing Starts (Thousands of Units)*	[illegible]	[illegible]	2,056	1,632
New Construction Expenditures*	[illegible]	[illegible]	$ 356.1r	$ 334.3
Total Business Inventories †	[illegible]	[illegible]	$ 584.0	$ 575.0
Total Business Sales †	[illegible]	[illegible]	$ 435.0	$ 417.4

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

So, too, growth in Europe is essential if U.S. manufacturers are to be able to take advantage of the decline in the dollar and narrow the existing 12-digit trade deficit. U.S. sales to Europe are no higher today than at the start of this decade, and the U.S. trade balance with the region has, not surprisingly, deteriorated sharply. Between 1981 and 1985, the U.S. trade balance with Western Europe shifted from a surplus of $13½ billion to a red-ink total of $23 billion—a $36½ billion adverse swing which, by itself, accounted for more than one third of the overall widening in the U.S. trade deficit between 1981 and 1985.

Finally, quicker European economic growth may arrest the ascent of unemployment rates throughout the region—which remain firmly riveted in double-digit territory in most countries. But perhaps even more important, it could produce the environment necessary for making the required changes both in labor laws and social programs if Europe's most intractable problem is to be more permanently overcome. European laws, for example, make it difficult for companies to lay off workers when times are bad, making employers reluctant to hire even when business is booming. Moreover, generous unemployment payments decrease the incentive for the jobless to seek work. While these rigidities will be slow to dissolve, what better time to meet them head-on than when economies are growing?

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (3/26/86)	162,062	94	+ 4,144
New York City (4/2/86)	35,043	– 724	+ 1,860
Commercial Paper (4/2/86)	300,411	+ 309	+50,629

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (3/26/86)	253,918	– 1,815	+ 1,580
New York City (4/2/86)	58,975	+ 1,340	– 3,013

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (3/26/86)	730,064	– 5,584	+ 64,417
New York City (4/2/86)	160,195	+ 411	+ 14,807

Financial Markets

	Friday 4/11/86	[illegible]	[illegible]
U.S. Governments, Closing Yields:			
90-Day Bills†	[illegible]	.30	– 2.17
180-Day Bills†	[illegible]	.24	– 2.44
Longest Bills†	[illegible]	.25	2.79
Recent Issues:			
7⅛s 3/31/88	[illegible]	.25	
7¼s 3/31/90	[illegible]	.25	
8⅞s 2/15/96	[illegible]	.18	
9¼s 2/15/16	[illegible]	.19	
Municipals:			
Bond Buyer—20 Bond Index* (4/10/86)	[illegible]	+ .10	2.14
Blue List Total ($ Millions)	[illegible]	+$ 275	+ $ 920
30-Day Visible Supply ($ Millions)	[illegible]	+$1,267	+ $ 685
Total	[illegible]	+$1,542	+ $1,605
Corporates:			
Moody's Aa Composite (4/10/86)	[illegible]	+ .05	3.62
30-Day Visible Supply ($ Millions)	[illegible]	–$3,915	+ $1,460
Stocks:			
Dow-Jones Averages:			
Industrials	[illegible]	+ 50.96	+ 524.50
Transportation	[illegible]	+ 6.74	+ 187.85
Utilities	[illegible]	+ 1.64	+ 32.31
65 Stocks	[illegible]	+ 14.42	+ 183.35
N.Y.S.E. Composite Index	[illegible]	+ 3.93	+ 31.58
N.Y.S.E. Avg. Daily Vol. for Week (000's)	[illegible]	+ 3,052	+ 58,156

* 46% Taxable equivalent 13.43%

† Bond equivalent.

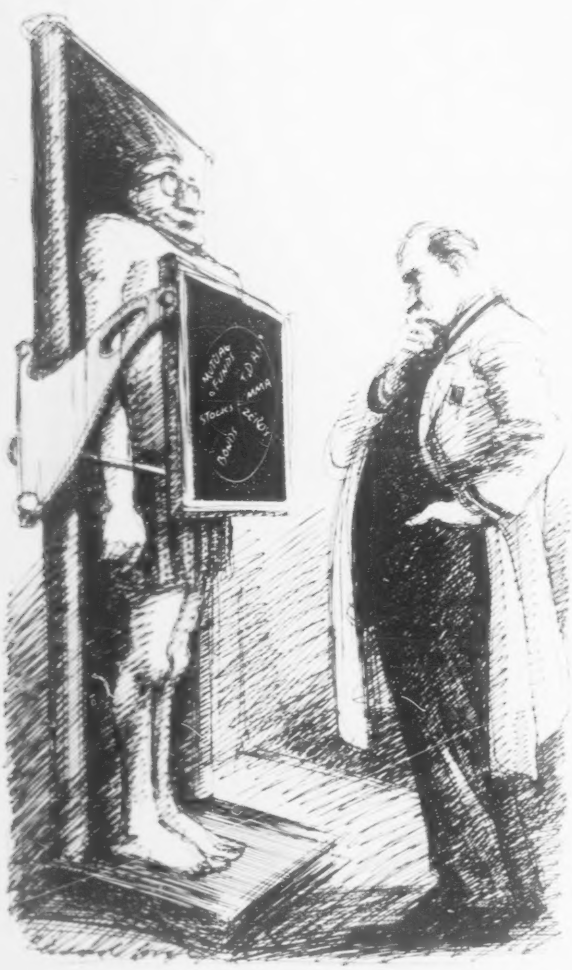
International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 4/11/86	Week Ago
Overnight	6.81%	7.19%
1 month	6.81	7.31
3 month	6.69	7.19
6 month	6.69	7.06
1 year	6.75	7.06
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.55%	7.86%
Long Term (7 to 15 yrs.)	8.14	8.30

FOREIGN EXCHANGE SPOT RATES

New York Opening (4/11/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02141	46.71
Canada	.7219	1.3853
Denmark	.1165	8.5850
France	.1363	7.3350
Germany	.4342	2.3033
Italy	.0006325	1581.00
Japan	.005610	178.25
Mexico	.002020	495.00
Netherlands	.3857	2.5930
Switzerland	.5173	1.9333
U.K.	1.4765	.6773

How healthy is your IRA?



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The Manufacturers Hanover

Financial Digest

Economic Commentary, Selected Financial Data, and Business Indicators

MONDAY, APRIL 28, 1986

VOLUME XXIII, NUMBER 10

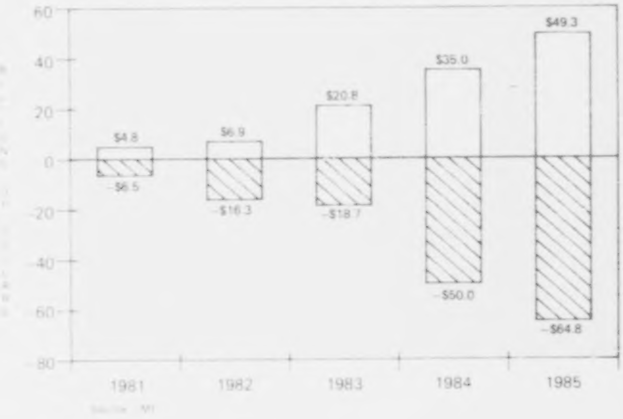
Japan's Trade Surplus Still Expands . . .

One of the major topics of discussion at the upcoming Tokyo summit meeting will be Japan's burgeoning trade surplus. For despite the export-dampening effects of the steep appreciation of the yen since the G-5 meeting on September 22, 1985, Japan's trade account is poised for its fourth consecutive record surplus this year. The structural nature of Japan's import composition helps to explain this phenomenon, as Japan is the world's largest importer of raw materials. Therefore, in light of the present depressed nature of world commodity prices, the terms of trade have turned decisively in its favor. In this regard, the steep fall in oil prices will be a significant factor boosting the surplus from $56 billion in 1985 to at least $70 billion this year. According to Prime Minister Nakasone, every $10 decline in oil prices will boost Japan's surplus by $12 billion annually.

Japan's export performance, on the other hand, has already weakened, reflecting the effects of the steep rise of the yen in recent months. All sectors except motor vehicles are performing poorly, particularly ships, steel and chemicals. However, when measured in dollar terms, as the government does in releasing the trade statistics, this export weakness has been masked by the appreciation of the yen. In fact, data for the first two months of 1986 reveal a respectable 17.1 percent year-over-year gain in exports when translated from the stronger yen back into now cheaper dollars. As a result, the trade surplus during the January-February period advanced by 50 percent to $7.2 billion. Such a trend will continue throughout 1986 as the volume decline in exports fails to match the yen's appreciation, thus boosting their dollar value.

Not surprisingly, the yen's ascent has generated significant concerns among the Japanese business community, given the threat to its international competitive position and the possibility of sharply diminished profits. To retain market share, especially in the important U.S. market which accounted for nearly 40 percent of total export sales during the first two months of 1986, Japanese companies are reducing their profit margins. Automobile manufacturers for example have announced price increases of four to ten percent in recent months, well below that suggested by the rise of the yen. The decline in oil prices, the fall in domestic interest rates and low inflation (just 1.8 percent during the year ending February) aid Japanese companies in their attempt to hold the line on export prices. Nonetheless, profit margins will shrink, particularly as falling export volumes coincide with weak domestic demand.

JAPAN: CURRENT ACCOUNT SURPLUS (CLEAR BAR) VS. NET LONG-TERM CAPITAL DEFICIT (SHADED BAR)



. . . Despite Sluggish Exports . . .

What is more, heightened sales competition from such newly industrialized countries (NICs) of Asia as Korea and Taiwan also clouds Japan's export outlook. While the yen has strengthened substantially, the currencies of its industrialized Asian neighbors have been relatively steady against the dollar. Both the Korean won and Taiwan dollar have risen only slightly against the U.S. currency since the turn of the year, and the Singapore dollar has actually eased modestly. Korea's international competitive position has been particularly enhanced by the yen's rise, as evidenced by the 19.5 percent increase in exports recorded during the first two months of the year. Steel, television sets and VCRs are among the many products which will greatly benefit from the yen's appreciation as Korea chips away at Japan's market share in these areas.

In addition to the rise of the yen and enhanced competitiveness from other Asian NICs, Japan's

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export performance will also be hindered by China's economic slowdown, initiated in order to narrow its trade deficit, particularly with Japan. Last year, China was Japan's second largest export market, absorbing a shade more than seven percent of Japan's total exports. However, with growth slowing in the People's Republic, Japanese exports dropped by eight percent during the first two months of 1986 compared with same-period, year-earlier levels, while the proportion of overall exports accounted for by China fell to five percent.

. . . Producing Additional Capital Outflows

Given the enormity of Japan's trade and current account surpluses, it is no surprise that this country has become the world's largest capital exporter—replacing OPEC, whose ability to export capital has diminished in tandem with the slump in oil prices. In 1985, for example, Japan's basic balance (which includes the current account plus net long-term capital flows) was deep in the red, by a hefty $15.5 billion, due to net long-term capital outflows of nearly $65 billion—which entirely offset the largest annual current account surplus ever posted by any country (see chart on page 1). What is more, this trend accelerated during the first two months of 1986, with the basic balance deficit ballooning by 330.7 percent to $9.4 billion from similar period, year-ago levels, as net long-term capital outflows surged from $5.5 billion to $15.2 billion.

Selected Federal Reserve Data

[illegible]

	Week Ending 4/23/86	[illegible]	[illegible]
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	187,163	+ 1,489	+14,891
Loans to Depository Inst.	.992	+ .263	− .126
Float	.357	+ .194	− .251
Total Reserve Bank Credit	204,320	+ 1,962	+18,143
Treasury Deposits with Federal Reserve Banks	7,221	− 1,172	− 3,795
Currency in Circulation	194,368	− .497	+13,552
Gov'ts held for Foreign Acct. by F.R. Banks (End of Week)	141,280	+ 1,467	+24,594
	4/23/86		
Member Bank Reserves:			
Total Reserves Held	48,063	+ 1,438	+ 6,169
Excess (Deficiency)	.956	+ .326	+ .072
Net Free Reserves	.756	+ .434	+ .274

Monetary Aggregates †		[illegible]	[illegible]
M1 (4/14/86)	641.5	+ 8.9‡	+ 11.8‡
M2 (March '86)	2,590.3	+ 3.8	+ 6.6
M3 (March '86)	3,258.6	+ 7.2	+ 7.0
Domestic Nonfinancial Debt (4th Q'85)	6,867.9	+ 19.2	+ 14.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 4/25/86	[illegible]	[illegible]	1 Year
‡ U.S. Treasury Bills	6.16%	6.19%	6.20%
* Federal Agencies	6.54	6.66	6.69
* Municipal Notes—High Grade (46% Taxable Equivalent)	8.70	7.87	8.15
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.52	6.52	6.50

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	6.62%	May	6.65%
15- 29 days	6.60	Jun.	6.55
30- 59 days	6.50	Jul.	6.55
60- 89 days	6.40	Aug.	6.50
90-179 days	6.20	Sep.	6.50
180-239 days	6.05	Oct.	6.40
240-270 days	6.05		

‡ Industrial Paper—Prime			
30- 89 days	6.50%	† Federal Funds Effective Rate	6.80%
90-120 days	6.45		

‡ Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

[illegible]

	[illegible]		[illegible]	Year Ago Period
Gross National Product (Current Dollars)*	1st Q 86	$ 4,117	$ 4,059	$ 3,918
Gross National Product (1982 Dollars)*	1st Q 86	$ 3,619	$ 3,591	$ 3,548
Percent Change, Annual Rate	1st Q 86	3.2	0.7	3.7
Change in Consumer Prices*	Mar 86	[illegible]	− 4.8%	6.0%
Change in Producer Prices*	Mar 86	[illegible]	− 19.2%	0.0%
Civilian Employment (Thousands of Persons)†	Mar 86	108,788	108,561	106,951
Unemployment as % of Civilian Labor Force†	Mar 86	7.2%	7.3%	7.3%
Personal Income*	Mar 86	$ 3,407	$ 3,401r	$ 3,258
Leading Indicators Composite Index (1967=100)†	[illegible]	[illegible]	174.1	167.4
Industrial Production Index (1977=100) †	Mar 86	[illegible]	125.7	124.0
Net Change in Consumer Installment Credit †	Feb 86	[illegible]	$ 7.66r	$ 9.04
U.S. Merchandise Trade Balance †	Feb 86	[illegible]	−$ 14.42	−$ 11.45
Plant and Equipment Expenditures*	[illegible]	[illegible]	$390.66(a)r	$387.83r
Private Housing Starts (Thousands of Units)*	Mar 86	[illegible]	1,997r	1,849
New Construction Expenditures*	Feb 86	[illegible]	$ 356.1	$ 334.3
Total Business Inventories †	Feb 86	[illegible]	$ 585.0r	$ 578.5r
Total Business Sales †	Feb 86	$ 427.2	$ 432.0r	$ 418.2r

*Seasonally adjusted annual rate. †Seasonally adjusted. [illegible] r Revised. a Anticipated.

The bulk of Japan's overseas investments are in long-term government bonds, mainly in the United States. But Canada, Australia and New Zealand as well are also key recipients of such flows, and interest is increasing in West Germany. During the first two months of 1986 alone, Japan's net purchases of foreign bonds totaled nearly $12 billion, suggesting that the full-year figure could be about $70 billion. In contrast to bonds, net purchases of stock have so far been rather meager, totaling just $510 million during this period.

Despite the yen's strength, Japan's appetite for dollar-denominated assets has not abated and, in fact, is expected to swell as there is simply no other market in the world which can accommodate its growing current account surplus. No financial center can match the depth and resiliency of the U.S. financial markets, whose attractiveness has been enhanced by a pattern of interest rate differentials favoring dollar asset acquisition. In addition, the sharp appreciation of the yen makes investment in the U.S. less expensive. Finally, the Japanese government's recent decision to lift the limit of assets held by life insurance companies in foreign securities from ten to 25 percent also will encourage capital outflows. Indeed, Japan will see its position as the world's principal capital exporter grow in coming years—the often overlooked flip side of its hefty trade surpluses.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (4/9/86)	159,200	– 228	+ 2,921
New York City (4/16/86)	34,834	+ 177	+ 1,853
Commercial Paper (4/16/86)	298,703	+ 1,485	+46,706

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (4/9/86)	258,575	– 2,619	+ 2,859
New York City (4/16/86)	59,041	+ 1,022	– 2,885

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (4/9/86)	726,812	– 5,654	+ 60,188
New York City (4/16/86)	160,463	+ 2,786	+ 13,919

Financial Markets

	Friday 4/25/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.29%	+ .29	– 1.75
180-Day Bills†	6.46	+ .41	– 2.01
Longest Bills†	6.61	+ .47	– 2.29
Recent Issues:			
6 5/8s 4/30/88 (When Issued)	6.90	NA	
7 1/4s 3/31/90	7.27	+ .67	
8 7/8s 2/15/96	7.56	+ .51	
9 1/4s 2/15/16	7.60	+ .43	
Municipals:			
Bond Buyer—20 Bond Index* (4/24/86)	7.22%	+ .06	– 2.17
Blue List Total ($ Million)	$1,968	+ $188	+ $ 426
30-Day Visible Supply ($ Million)	$5,690	+ $287	+ $1,360
Total	$7,658	+ $475	+ $1,786
Corporates:			
Moody's Aa Composite (4/24/86)	9.33%	– .22	– 3.27
30-Day Visible Supply ($ Million)	[illegible]	+ $188	+ $2,338
Stocks:			
Dow-Jones Averages:			
Industrials	[illegible]	4.83	+ 560.39
Transportation	[illegible]	1.59	+ 224.72
Utilities	[illegible]	5.08	+ 31.95
65 Stocks	713.84	– 4.30	+ 199.86
N.Y.S.E. Composite Index	139.51	– .36	+ 33.99
N.Y.S.E. Avg. Daily Vol. for Week (000's)	147,374	+ 3,524	+ 50,460

* 46% Taxable equivalent 13.37%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 4/25/86	Week Ago
Overnight	6.69%	6.56%
1 month	6.88	6.56
3 month	6.81	6.50
6 month	6.81	6.50
1 year	6.88	6.50
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.74%	7.40%
Long Term (7 to 15 yrs.)	8.33	8.00

FOREIGN EXCHANGE SPOT RATES

New York Opening (4/25/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02255	44.35
Canada	.7219	1.3852
Denmark	.1244	8.0375
France	.1448	6.9050
Germany	.4625	2.1620
Italy	.0006734	1485.00
Japan	.005976	167.35
Mexico	.001969	508.00
Netherlands	.4076	2.4535
Switzerland	.5536	1.8065
U.K.	1.5505	.6450

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- For more information call (914) 967-5356.

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The Manufacturers Hanover Financial Digest

Economic Commentary, Selected Financial Data, and Business Indicators

MONDAY, MAY 12, 1986

VOLUME XXIII, NUMBER 11

America Honors Small Business . . .

Next week, the nation will once again be honoring its entrepreneurial spirit with the celebration of Small Business Week. For seven days, beginning May 18, attention will be given to the establishments that dominate our economy—and our lives—every day of the year. Only in this country is the entrepreneurial spirit so entrenched. There are about 15.2 million nonfarm businesses in the U.S. today, and of these, 99 percent are considered small business enterprises. In particular, the current business expansion has sparked an extraordinarily high degree of entrepreneurial activity. The number of new business incorporations, for example, set a record in 1985 at 670,000—5.4 percent above the 1984 level and 26 percent above the number of new incorporations in 1980.

In fact, the small business economy is so much a part of everyday life that it is easily overlooked. Small companies are deeply rooted in every local community and neighborhood and provide entry-level jobs for teenagers, women, minorities and immigrants. Their contributions to the nation's economic health are significant: Small businesses develop new products and services and provide new jobs, technological innovations, entrepreneurial initiative, managerial talent, new skills and training—not to mention spurring older, established companies to greater efficiency and more competitiveness. Small companies are more flexible than their large counterparts in making fast decisions on products and pricing, and they are usually more adept in making their employees feel more integral to the company's success than their large counterparts are able to do.

Small businesses give the United States an economic vitality no other country can claim. In terms of numbers, they employ almost half of the nation's private nonfarm workers, contribute 42 percent of all sales, and generate approximately 38 percent of the gross national product. In fact, small businesses have become the main driving force behind the nation's economic growth. From 1970 to 1980, small businesses provided the largest chunk of the 20 million new jobs generated. What is more, this trend has accelerated during the 1980s. Even during 1981 and 1982, when the worst recession in decades caused massive layoffs in the steel, auto and other basic industries, small businesses posted a relatively strong performance, demonstrating their ability to adapt and grow in times of economic adversity and providing a moderating force. According to the Small Business Administration (SBA), small businesses created a total of over 2.6 million new jobs during 1981 and 1982, more than offsetting the 1.7 million positions lost by larger businesses—a net gain of 984,000 new jobs.

. . . For Its Many Contributions

The current economic expansion has created opportunities for employment growth for small and large companies alike, but large businesses have not kept up with the employment gains of small companies. In the 12 months ending September, 1985, small businesses increased their payrolls by nearly six percent, while large companies boosted theirs by only 0.6 percent. This year, small businesses again will do most of the hiring, according to a survey by Dun & Bradstreet Corporation. Nearly two thirds of the three million new jobs that businesses plan to create this year will be generated by companies that employ fewer than 100 workers.

There is another reason besides job creation that America's small businesses should be saluted for—namely, innovation. Small entrepreneurs have traditionally been the major innovators in American business. Smaller companies tend to create more new products and services. According to the SBA, small businesses have introduced two and a half times as many innovations as large companies relative to the number of people employed and have launched new industries ranging from semiconductors to gene splicing. Often, small companies spur their larger rivals to develop new strategies. These innovations keep U.S. companies more competitive at home and abroad.

Long Island Prospers

One example of how an economy which is dominated by small business can prosper is Long Island, a suburb of New York City. Nine out of every ten companies in Long Island employ fewer than 20 people and these companies generate the preponderance of employment growth. With 1.1 million jobs

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in 1985, nonagricultural employment was at a record level. A total of 40,000 new jobs was added to payrolls last year, on the heels of a record 53,000 new positions created in 1984. The gains were posted across the entire employment spectrum. Even manufacturing employment, which nationally has been in its own mini-recession, generated more than 3,000 new positions—an increase of 1.8 percent from 1984. Although this gain was substantially below the increase in factory employment that took place in 1984 when more than 9,000 new factory jobs were created, it compares with an increase of only 0.1 percent in factory employment nationally, and declines of 5.2 percent in neighboring New York City and 2.3 percent in New York State.

The strong growth in employment allowed Long Island to enjoy one of the lowest unemployment rates in the country. At 4.4 percent last year, it compared with a jobless rate of 7.2 percent nationwide, 6.5 percent in New York State and 8.1 percent in neighboring New York City.

Long Island's economic vitality is even more dramatic when viewed in perspective. Early in the 1980s, the U.S. suffered two back-to-back recessions which, by some measures, were the most severe in the postwar period. The Long Island economy came through literally unscathed, as it continued to create new jobs. The Long Island counties of Nassau and Suffolk have added more than 173,000 jobs so far in

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 5/7/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	190.972	+ 3.936	+ 9.677
Loans to Depository Inst.	.905	– .152	+ .271
Float	.644	+ .123	– .052
Total Reserve Bank Credit	209.066	+ 4.378	+13.474
Treasury Deposits with			
Federal Reserve Banks	7.246	+ .477	– 5.311
Currency in Circulation	195.248	+ 1.217	+13.332
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	145.787	– .214	+28.276
	5/7/86		
Member Bank Reserves:			
Total Reserves Held	47.753	– .796	+ 7.233
Excess (Deficiency)	.928	+ .047	+ .229
Net Free Reserves	.584	– .107	+ .442
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates†			
M1 (4/28/86)	648.6	+ 11.3‡	+ 12.1‡
M2 (March '86)	2,590.4	+ 3.8	+ 6.6
M3 (March '86)	3,258.1	+ 7.2	+ 6.9
Domestic Nonfinancial Debt (4th Q'85)	6,867.9	+ 19.2	+ 14.7

†Seasonally adjusted.

* Seasonally adjusted annual rate.

‡ Four-week moving average.

New York Money Market

Offering Rates 5/9/86	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	6.08%	6.09%	6.13%
* Federal Agencies	6.32	6.32	6.35
* Municipal Notes—High Grade (46% Taxable Equivalent)	7.41	7.69	7.87
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.48	6.50	6.55

‡Finance Company Paper—Prime	
5- 14 days	6.65%
15- 29 days	6.62
30- 59 days	6.60
60- 89 days	6.55
90-179 days	6.35
180-239 days	6.05
240-270 days	6.05

‡* Bankers' Acceptances	
Jun.	6.65%
Jul.	6.60
Aug.	6.55
Sep.	6.50
Oct.	6.45
Nov.	6.40

‡Industrial Paper—Prime	
30- 89 days	6.55%
90-120 days	6.45

†Federal Funds Effective Rate	6.80%

‡Discount basis. • Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'86	$ 4,117	$ 4,059	$ 3,918
Gross National Product (1982 Dollars)*	1st Q'86	$ 3,619	$ 3,591	$ 3,548
Percent Change, Annual Rate	1st Q'86	3.2	0.7	3.7
Change in Consumer Prices*	Mar '86	– 4.8%	– 4.8%	6.0%
Change in Producer Prices*	Mar '86	– 13.2%	– 19.2%	0.0%
Civilian Employment (Thousands of Persons)†	Apr '86n	108,892	108,788	106,872
Unemployment as % of Civilian Labor Force†	Apr '86n	7.1%	7.2%	7.3%
Personal Income*	Mar '86	$ 3,407	$ 3,401	$ 3,258
Leading Indicators Composite Index (1967=100)†	Mar '86n	176.6	175.7r	167.6
Industrial Production Index (1977=100)†	Mar '86	125.1	125.7	124.0
Net Change in Consumer Installment Credit†	Feb '86	$ 4.97	$ 7.66	$ 6.85r
U.S. Merchandise Trade Balance†	Mar '86n	–$ 14.52	–$ 11.37	–$ 10.14
Plant and Equipment Expenditures*	2nd Q'86	$400.68(a)	$390.66(a)	$387.83
Private Housing Starts (Thousands of Units)*	Mar '86	1,949	1,997	1,849
New Construction Expenditures*	Mar '86n	$ 354.6	$ 358.9r	$ 333.7
Total Business Inventories†	Feb '86	$ 585.1	$ 585.0	$ 578.5
Total Business Sales†	Feb '86	$ 427.2	$ 432.0	$ 418.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

this decade, a 19.3 percent gain and more than double the national rise of 8.8 percent. Employment in New York State as a whole rose only eight percent in the same period. Long Island's employment increase so far in the 1980s is only 20,000 jobs short of the rise generated throughout the entire decade of the 1970s!

The most surprising development is the resurgence in manufacturing. About 16,000 new factory jobs have been created in Nassau and Suffolk thus far in the 1980s, in contrast to the decline in the nation and in many other parts of New York State. For example, 1.6 million factory jobs nationwide have disappeared so far in this decade.

The underlying strength of the Long Island economy is reflected in New York State's index of business activity. At the end of last year, Nassau and Suffolk's index stood at 211, up from 198 a year earlier, and it was higher than the indexes of any other area within New York State. Since the index, which is prepared by the New York State Department of Commerce, uses 1967 as its base year, it, in effect, demonstrates how rapidly the Long Island economy has grown in the past 19 years. And in fact, it shows that the bi-county's economy enjoyed the fastest growth in the state during the 1967-1985 period.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (4/23/86)	156,861	– 91	– 21
New York City (4/30/86)	34,891	+ 489	+ 1,345
Commercial Paper (4/30/86)	300,361	– 536	+44,346

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (4/23/86)	258,842	– 2,644	+ 3,636
New York City (4/30/86)	57,988	+ 473	– 4,075

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (4/23/86)	734,286	– 936	+ 64,139
New York City (4/30/86)	161,533	+ 1,506	+ 12,540

Financial Markets

	Friday 5/9/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.22%	– .06	– 1.76
180-Day Bills†	6.33	– .05	– 1.98
Longest Bills†	6.46	– .06	– 2.25
Recent Issues:			
6⅝s 4/30/88	6.83	– .02	
7¼s 3/31/90	7.13	– .01	
7⅜s 5/15/96 (When Issued)	7.48	NA	
7¼s 5/15/16 (When Issued)	7.39	NA	
Municipals:			
Bond Buyer–20 Bond Index* (5/7/86)	7.36%	+ .03	– 1.75
Blue List Total ($ Million)	$2,262	+ $ 34	+ $ 583
30-Day Visible Supply ($ Million)	$4,923	– $462	+ $1,998
Total	$7,185	– $428	+ $2,581
Corporates:			
Moody's Aa Composite (5/7/86)	9.31%	– .02	– 3.28
30-Day Visible Supply ($ Million)	$3,620	+ $ 35	+ $2,985
Stocks:			
Dow-Jones Averages:			
Industrials	1,789.43	+ 14.75	+ 515.25
Transportation	788.03	+ 1.47	+ 171.00
Utilities	182.91	+ 1.50	+ 23.18
65 Stocks	695.81	+ 4.56	+ 172.36
N.Y.S.E. Composite Index	137.12	+ 1.73	+ 30.48
N.Y.S.E. Avg. Daily Vol. for Week (000's)	125,382	–13,186	+ 17,502

* 46% Taxable equivalent 13.63%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 5/9/86	Week Ago
Overnight	6.75%	6.81%
1 month	6.81	6.88
3 month	6.75	6.81
6 month	6.75	6.81
1 year	6.81	6.88
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.60%	7.60%
Long Term (7 to 15 yrs.)	8.00	8.25

FOREIGN EXCHANGE SPOT RATES **New York Opening (5/9/86)**	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02249	44.47
Canada	.7245	1.3802
Denmark	.1238	8.0800
France	.1441	6.9375
Germany	.4592	2.1775
Italy	.0006682	1496.50
Japan	.006175	161.95
Mexico	.001927	519.00
Netherlands	.4078	2.4520
Switzerland	.5514	1.8135
U.K.	1.5405	.6491

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- For more information call (914) 967-5356.

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Financial
Digest
Economic Commentary,
Selected Financial Data,
and Business Indicators

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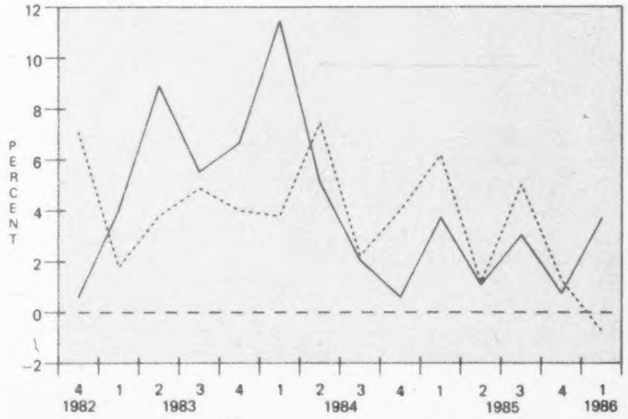
Despite Economic Sluggishness . . .

In recent weeks, the financial markets have been buffeted by the crosscurrents of a less than robust pace of business here and abroad, a pronounced acceleration of money supply growth, a decided firming of oil prices and heightened concerns over the downside vulnerability of the dollar in the foreign exchange markets. In light of this array of factors—some suggesting the need for more monetary ease, others suggesting the opposite—the Federal Reserve's policy-setting Federal Open Market Committee probably decided at this week's meeting to walk a fine line between the two, recognizing that while business conditions preclude a firming of the monetary reins, dollar concerns preclude an easing. This suggests that any monetary policy change will be put on hold for now, while the central bank awaits more definitive signs of the economy's response to the easing actions already taken.

To be sure, an ample array of mixed economic signals adds to the usual uncertainty surrounding both the future growth pace and the appropriate posture of monetary policy. Take, for example, the real GNP growth rate. Despite widespread predictions to the contrary, the Commerce Department revised upward its estimate of the first quarter, inflation-adjusted growth rate, from a preliminary 3.2 percent annual rate to a seemingly healthier 3.7 percent annual clip—the strongest advance in a year. At first glance, the economy would appear to be perking up from last year's lethargy, needing little further monetary stimulation. But, as is often the case, first appearances can be deceiving. For when the GNP-boosting effect of a hefty buildup of business inventories is netted out, a somewhat different picture emerges: The first quarter-over-quarter drop in inflation-adjusted final sales (GNP minus the change in inventories) since the onset of the current business expansion 3½ years ago (see chart).

Indeed, although a pickup in business activity had been expected by now due to tumbling oil prices and interest rates, few signs of this are readily apparent. While the unemployment rate moved a tenth of a percentage point lower in April, payroll employment rose only modestly; all of the jobs gains were concentrated in the services-construction side of the economy, while manufacturing employment continued to drop. So, too, the recent upturn in auto sales and the surge in housing starts have been offset, to some extent, by the generally lackluster pace of nonauto retail sales and the ongoing malaise in the manufacturing sector. While the ingredients of a business upturn are certainly in place—interest rates at their lowest levels in nearly a decade and the dollar's external value now well below the highs reached a year ago—signs of either a consumer-led, or export-led acceleration of growth have yet to materialize.

REAL GNP (LINE) VS. REAL FINAL SALES (DOT)
(QUARTER-OVER-QUARTER PERCENT CHANGE AT ANNUAL RATE)



. . . Other Concerns . . .

Nor is the United States the only country awaiting an as yet unrealized business upturn. In Germany, a barrage of weak, March economic statistics—ranging from a drop in domestic and foreign factory orders to another monthly decline in industrial production—point to a pace of business considerably weaker than originally anticipated. Real GNP growth apparently stalled in the first quarter—and may have actually eased—while the unemployment rate remains in the nine percent zone. What is more, the dimming of German growth prospects clouds the outlook for much of the rest of Western Europe—already prompting France to scale back its 1986 growth expectations. Add to this the fact that industrial production in March eased in both Japan and the United Kingdom, and a picture emerges of soft business conditions throughout a large part of the industrial world.

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While it could reasonably be expected that industrial country central banks will respond to such business conditions with more monetary policy ease, the timing of such a move, especially in the United States, is more uncertain than usual. For it will depend not only on the second quarter's economic numbers, but also the degree of the Fed's concern over two other things: First, the sharp acceleration in money supply growth now underway and second, the downside vulnerability of the dollar in the foreign exchange markets. In each instance, there are risks associated with another turn toward more monetary ease.

The growth of the M1 money supply, for example, has accelerated sharply in recent weeks, advancing at a nearly 20 percent annual clip over the past four, while the growth of the broader M2 money supply has picked up as well. It rose by nearly $30 billion in April alone, placing its year-to-date growth back within its 1986 target range. Although the Fed continues to tolerate this trend—pumping liquidity into the banking system at a torrid clip— and will probably continue to do so until such time as the growth of M2 approaches its upper target boundary, there has to be some limit to this generosity, especially if inflation expectations are to remain in check.

. . . Could Preclude More Monetary Ease

So, too, if a downward slide of the dollar in the foreign exchange markets accompanies more ease

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending	$ Change Since	
	5/21/86	Week Ago	Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	188.359	+ 1.530	+ 15.641
Loans to Depository Inst.	.848	+ .042	− .626
Float	.396	− .392	− .195
Total Reserve Bank Credit	204.580	− .520	+ 18.530
Treasury Deposits with Federal Reserve Banks	3.972	− .619	+ .834
Currency in Circulation	196.453	+ .067	+ 13.416
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	148.311	+ 2.713	+ 29.124
	5/21/86		
Member Bank Reserves:			
Total Reserves Held	47.579	− .183	+ 6.857
Excess (Deficiency)	.739	− .139	− .113
Net Free Reserves	.483	− .051	+ .696
		% Change Since	
Monetary Aggregates†		Three Months Ago*	Year Ago
M1 (5/12/86)	656.0	+ 14.9‡	+ 12.6‡
M2 (April '86)	2,620.8	+ 8.0	+ 7.7
M3 (April '86)	3,287.7	+ 7.9	+ 7.7
Domestic Nonfinancial Debt (4th Q'85)	6,867.9	+ 19.2	+ 14.7

† Seasonally adjusted.

* Seasonally adjusted annual rate.

‡ Four-week moving average.

New York Money Market

Offering Rates 5/23/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	6.17%	6.23%	6.28%
* Federal Agencies	6.44	6.42	6.48
* Municipal Notes—High Grade (46% Taxable Equivalent)	7.41	7.04	7.69
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.70	6.70	6.80

‡ Finance Company Paper—Prime	
5- 14 days	6.73%
15- 29 days	6.75
30- 59 days	6.75
60- 89 days	6.75
90-179 days	6.60
180-239 days	6.30
240-270 days	6.30

‡* Bankers' Acceptances	
Jun.	6.78%
Jul.	6.70
Aug.	6.68
Sep.	6.65
Oct.	6.62
Nov.	6.60

‡ Industrial Paper—Prime	
30- 89 days	6.73%
90-120 days	6.65

† Federal Funds	
Effective Rate	6.85%

‡ Discount basis.

* Subject to availability.

† Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period			Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st	Q'86	$ 4,121r	$ 4,059	$ 3,918
Gross National Product (1982 Dollars)*	1st	Q'86	$ 3,624r	$ 3,591	$ 3,548
Percent Change, Annual Rate	1st	Q'86	3.7r	0.7	3.7
Change in Consumer Prices (all urban consumers)*	Apr	'86n	− 3.6%	− 4.8%	3.6%
Change in Producer Prices*	Apr	'86n	− 7.2%	−13.2%	6.0%
Civilian Employment (Thousands of Persons)†	Apr	'86	108,892	108,788	106,872
Unemployment as % of Civilian Labor Force†	Apr	'86	7.1%	7.2%	7.3%
Personal Income*	Apr	'86n	$ 3,447	$ 3,407	$ 3,289
Leading Indicators Composite Index (1967 = 100)†	Mar	'86	176.6	175.7	167.6
Industrial Production Index (1977 = 100)†	Apr	'86n	125.1	124.9r	124.1
Net Change in Consumer Installment Credit †	Mar	'86n	$ 3.71	$ 5.02r	$ 8.30r
U.S. Merchandise Trade Balance †	Mar	'86	−$ 14.52	−$ 11.37	−$ 10.14
Plant and Equipment Expenditures*	2nd	Q'86	$400.68(a)	$390.66(a)	$387.83
Private Housing Starts (Thousands of Units)*	Apr	'86n	2,009	1,930r	1,851
New Construction Expenditures*	Mar	'86	$ 354.6	$ 358.9	$ 333.7
Total Business Inventories †	Mar	'86n	$ 587.7	$ 585.2	$ 578.4
Total Business Sales †	Mar	'86n	$ 420.3	$ 427.2	$ 420.3

***Seasonally adjusted annual rate.** **†Seasonally adjusted.** **n-Newly reported figure.** **r-Revised.** **a-Anticipated.**

and lower interest rates, this, too, would complicate the Fed's inflation-fighting objectives—producing such commonly cited negatives as import price increases and, perhaps, diminishing the appetite of Japanese financial institutions for dollar-denominated assets. But, in this environment, it could also lead to something else, namely, the possible unraveling of the entire Group of Seven (G-7) framework. Japanese and German policymakers are becoming increasingly vocal in their concern over the negative consequences of the ongoing appreciation of their currencies relative to the dollar. After relying for years on export-led growth, this prop is fast disappearing with little emerging to replace it. Any unilateral switch to more ease here, without similar foreign steps, could hasten the dollar's descent, and further cloud business prospects in Japan and Germany.

Thus, while global business conditions may well warrant more monetary ease, these steps must be undertaken in a way that produces a balanced, global business upswing—not one which has one country benefiting at the expense of another. For the Fed, already wary of the acceleration in money growth, this means holding policy steady for another month or two, marking time as it awaits the response of the economy here, and those abroad, to actions already taken. If, at that time, the pace of global business remains soft, more ease and lower short-term interest rates are a good bet—not in isolation, but in tandem with the other industrial countries. H

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (5/7/86)	155,948	– 126	– 220
New York City (5/14/86)	34,487	– 197	+ 645
Commercial Paper (5/14/86)	307,816	+ 3,894	+49,563

Bank Loans

(Millions of Dollars)

Commerical and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (5/7/86)	261,509	+ 545	+ 4,253
New York City (5/14/86)	58,087	+ 110	– 4,465

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (5/7/86)	733,804	– 5,148	+59,246
New York City (5/14/86)	157,561	– 876	+ 9,841

Financial Markets

	Friday 5/23/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.33%	– .04	– 1.06
180-Day Bills†	6.50	– .05	– 1.25
Longest Bills†	6.67	– .10	– 1.48
Recent Issues:			
7⅛s 5/31/88 (When Issued)	7.14	NA	
7¼s 3/31/90	7.57	– .16	
7⅜s 5/15/96	7.86	– .11	
7¼s 5/15/16	7.46	– .19	
Municipals:			
Bond Buyer—20 Bond Index* (5/22/86)	7.78%	+ .25	– 1.13
Blue List Total ($ Million)	$2,130	– $ 105	+ $ 238
30-Day Visible Supply ($ Million)	$3,679	– $1,547	+ $ 494
Total	$5,809	– $1,652	+ $ 732
Corporates:			
Moody's Aa Composite (5/22/86)	9.52%	+ .08	– 2.60
30 Day Supply ($ Million)	$3,292	+ $192	+ $2,784
Stocks:			
Dow-Jones Averages:			
Industrials	1,823.29	+ 63.49	+ 521.32
Transportation	797.96	+ 26.26	+ 170.41
Utilities	184.35	+ 3.30	+ 22.37
65 Stocks	706.71	+ 22.53	+ 173.16
N.Y.S.E. Composite Index	138.88	+ 4.44	+ 30.01
N.Y.S.E. Avg. Daily Vol. for Week (000's)	118,280	– 6,074	+ 5,336

* 46% Taxable equivalent 14.41%

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 5/23/86	Week Ago
Overnight	6.62%	6.75%
1 month	6.94	6.94
3 month	6.94	6.94
6 month	6.94	7.00
1 year	7.13	7.13
EURODOLLAR BONDS Average Yield		
Medium Term (5 to 7 yrs.)	8.15%	7.90%
Long Term (7 to 15 yrs.)	8.50	8.30

FOREIGN EXCHANGE SPOT RATES

New York Opening (5/23/86)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.02150	46.52
Canada	.7334	1.3635
Denmark	.1192	8.3900
France	.1377	7.2600
Germany	.4389	2.2785
Italy	.0006400	1562.50
Japan	.005894	169.65
Mexico	.001843	542.50
Netherlands	.3902	2.5630
Switzerland	.5289	1.8908
U.K.	1.4915	.6705

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The Manufacturers
Hanover
Financial
Digest
Economic Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, JUNE 9, 1986
VOLUME XXIII, NUMBER 13

A Strong Year For Housing . . .

Amid the array of mixed economic indicators released recently, one definite bright spot is the housing sector. Rising personal incomes, relatively stable home prices and mortgage interest rates near 10 percent have combined to lift the number of new single-family homes sold in the March-April period to a record 878,000 units at a seasonally adjusted annual rate. The previous two-month high was the May-June 1978 rate of 861,000 units. Not surprisingly, this rapid sales pace has led to a surge in new-home construction. The seasonally adjusted monthly average rate of housing starts during the January-April period of this year was an impressive two million units. This is the highest four-month average since late 1978, when mortgage interest rates were also around 10 percent.

The main force behind the strength in residential construction would seem to be lower mortgage interest rates. According to a nationwide survey conducted by the Federal Home Loan Bank Board, the average effective fixed mortgage interest rate (the original contract rate adjusted for initial fees and charges) in early April was about 10½ percent. This was the lowest mortgage interest rate in seven years. Further, the drop in fixed-rate mortgages has narrowed the gap between conventional fixed-rate mortgages and adjustable rate mortgages (ARMs). The latest figures show ARMs less than one percentage point below fixed rates. This is quite a change from the 2¼ percentage point spread that existed less than two years ago. Accordingly, the popularity of ARMs has faded, with their share of total loans down to 29 percent—the lowest rate since May 1983 and less than half the almost 70 percent share seen in August 1984.

. . . Supported By Improved Affordability . . .

In less than two years, mortgage interest rates have dropped about five percentage points, shaving about $250 per month off the average monthly mortgage payment on a 30-year mortgage for a median-priced new single-family home. What this translates into is greatly improved housing affordability. One measure of this, the housing affordability index, compiled by the National Association of Realtors, is at its highest level since 1979. Another estimate places the percent of households that can now afford to buy their first home at 40 percent—the highest figure since early 1979.

This surge in housing construction is expected to continue throughout 1986 with total housing starts for the year likely to reach 2.1 million units. One of the reasons for continued optimism about the strength of residential construction is that the supply of unsold new homes is very lean. At April's selling pace, the inventory of unsold new homes was only 4.7 months—the lowest level in almost 15 years and almost three months less than the recent peak in late 1984. This low an inventory level near the start of the traditional busy summer season should support a strong summer and fall for new-home construction, since builders can worry less about oversupply. What is more, mortgage interest rates may not have bottomed out yet, and when they do, they are not expected to rise rapidly in the near future.

An indicator of future construction, building permits were at their highest level in over two years in April. Most of the month's increase came in the single-family home category, with permits for this type of unit jumping more than nine percent, month-over-month. Permits for multi-family dwellings fell almost six percent during the same period. In the first four months of this year, single-family starts comprised 63 percent of total starts but accounted for almost 80 percent of the increase from the immediately preceding four-month period. Construction of multi-unit dwellings has been experiencing a slowdown in growth from 1985's strong showing due to less attractive depreciation schedules and other factors involved in the various tax reform plans.

Finally, consumer confidence is high. The University of Michigan's survey of consumer sentiment shows a record number of households with favorable attitudes towards buying homes over the past four months. And, according to the Conference Board's survey of consumer attitudes and buying plans, the number of households planning to buy a home in the next six months is the highest since 1978.

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. . . Bolsters Demand In Many Industries

The vigor in the housing industry is important to the economy in general because it affects so many other industries. It is particularly significant now because other sectors of the economy are still experiencing lackluster growth. The ripples from the housing boom benefit manufacturers of such construction materials as lumber, gypsum, roofing and glass. Homebuilding also aids those manufacturers who produce finished products, including major appliances, cabinets, and bathroom fixtures, to name a few.

What is more, these industries are also getting a boost from two other areas. First, there is an extremely strong resale market for existing homes. Existing single-family home sales topped 3.5 million units at a seasonally adjusted annual rate in April—the highest reading since late 1979. Second, spending on home improvement, after adjusting for inflation, is at a record level. In the first quarter of this year, consumers spent over $29 billion at a seasonally adjusted annual rate on additions and alterations to existing homes. Both these items translate into increased demand for many types of home furnishings, fixtures and construction materials.

For example, in April, 3.7 million major household appliances were shipped, establishing a new record

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 6/4/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	190.114	+ 2.528	+16.470
Loans to Depository Inst.	.852	– .038	– 1.009
Float	.491	– .465	+ .347
Total Reserve Bank Credit	206.523	+ 2.097	+19.257
Treasury Deposits with Federal Reserve Banks	2.687	– .893	+ .287
Currency in Circulation	198.047	+ .863	+13.141
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	147.642	+ .574	+25.439
	6/4/86		
Member Bank Reserves:			
Total Reserves Held	47.870	+ .266	+ 7.240
Excess (Deficiency)	1.074	+ .346	+ .251
Net Free Reserves	.769	+ .297	+ .550
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates †			
M1 (5/26/86)	660.5	+ 17.3‡	+ 13.0‡
M2 (April '86)	2,621.6	+ 8.2	+ 7.7
M3 (April '86)	3,288.8	+ 8.2	+ 7.8
Domestic Nonfinancial Debt (1st Q'86)	7,033.5	+ 8.7	+ 14.2

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 6/6/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	6.45%	6.47%	6.52%
* Federal Agencies	6.60	6.58	6.58
* Municipal Notes—High Grade (46% Taxable Equivalent)	7.87	7.87	8.33
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.82	6.85	7.15

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	6.77%	Jul.	6.85%
15- 29 days	6.80	Aug.	6.80
30- 59 days	6.78	Sep.	6.80
60- 89 days	6.75	Oct.	6.80
90-179 days	6.70	Nov.	6.75
180-239 days	6.60	Dec.	6.70
240-270 days	6.55		

‡ Industrial Paper—Prime			
30- 89 days	6.80%	† Federal Funds Effective Rate	6.85%
90-120 days	6.75		

‡ Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'86	$ 4,121	$ 4,059	$ 3,918
Gross National Product (1982 Dollars)*	1st Q'86	$ 3,624	$ 3,591	$ 3,548
Percent Change, Annual Rate	1st Q'86	3.7	0.7	3.7
Change in Consumer Prices*	Apr '86	– 3.6%	– 4.8%	3.6%
Change in Producer Prices*	Apr '86	– 7.2%	– 13.2%	6.0%
Civilian Employment (Thousands of Persons) †	May '86n	109,110	108,892	106,939
Unemployment as % of Civilian Labor Force †	May '86n	7.3%	7.1%	7.3%
Personal Income*	Apr '86	$ 3,447	$ 3,408 r	$ 3,289
Leading Indicators Composite Index (1967=100) †	Apr '86n	179.2	176.6	166.7
Industrial Production Index (1977=100) †	Apr '86	125.1	124.9	124.1
Net Change in Consumer Installment Credit †	Apr '86n	$ 4.16	$ 3.09 r	$ 7.54
U.S. Merchandise Trade Balance †	Apr '86n	–$ 12.07	–$ 12.18 r	–$ 12.11
Plant and Equipment Expenditures*	2nd Q'86	$400.68 (a)	$390.66 (a)	$387.83
Private Housing Starts (Thousands of Units)*	Apr '86	2,009	1,930	1,851
New Construction Expenditures*	Apr '86n	$ 356.7	$ 353.9 r	$ 341.9
Total Business Inventories †	Mar '86	$ 587.7	$ 585.2	$ 578.4
Total Business Sales †	Mar '86	$ 420.3	$ 427.2	$ 420.3

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

for the month, according to the Association of Home Appliance Manufacturers (AHAM). Year-to-date shipments are about two percent higher than the record level set in the same period in 1985. This pattern is likely to continue throughout 1986 for two main reasons. First, the AHAM estimates that each new home built needs an average of three new major appliances, so the expected pace of housing starts should translate into at least six million appliances. Second, there is a potential for significant replacement demand for appliances due to extremely strong purchases throughout the early 1970s. The Conference Board reports that the number of consumers planning to buy a new major appliance in the next six months has been running at a strong pace for several months.

A number of other industries are experiencing a pick-up in their shipments as well. Many companies that supply items used in new homes recently reported year-over-year shipment gains of between 10 and 30 percent for the first quarter of this year. And, not only are these primary suppliers enjoying improvement, but increased secondary spending connected with buying a new home, such as landscaping, lawyers' fees, title insurance, furniture and other items, is also filtering through the economy. One study by the National Association of Realtors suggests that each new-home sale generates about $90,000 in related economic activity.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (5/21/86)	155,729	− 249	− 504
New York City (5/28/86)	34,288	− 506	+ 961
Commercial Paper (5/28/86)	310,155	− 945	+50,099

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (5/21/86)	258,910	− 2,012	+ 3,095
New York City (5/28/86)	56,696	+ 58	− 4,723

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (5/21/86)	738,416	+ 4,605	+ 62,030
New York City (5/28/86)	159,349	− 1,227	+ 13,549

Financial Markets

	Friday 6/6/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.49%	+ .07	− .89
180-Day Bills†	6.66	+ .01	− .97
Longest Bills†	6.82	+ .02	− 1.17
Recent Issues:			
$7\frac{1}{8}$s 5/31/88	7.28	− .02	
$7\frac{1}{4}$s 3/31/90	7.70	−0−	
$7\frac{3}{8}$s 5/15/96	7.99	− .04	
$7\frac{1}{4}$s 5/15/16	7.70	− .01	
Municipals:			
Bond Buyer—20 Bond Index* (6/5/86)	7.97%	+ .27	− .63
Blue List Total ($ Million)	$2,128	+$ 19	+ $ 350
30-Day Visible Supply ($ Million)	$4,522	+$ 807	+ $1,002
Total	$6,650	+$ 826	+ $1,352
Corporates:			
Moody's Aa Composite (6/5/86)	9.56%	+ .05	− 1.87
30-Day Visible Supply ($ Million)	$4,345	+$1,480	+ $3,367
Stocks:			
Dow-Jones Averages:			
Industrials	1,885.90	+ 9.19	+ 556.26
Transportation	795.38	− 7.98	+ 135.55
Utilities	187.76	− 1.86	+ 23.93
65 Stocks	721.84	− .85	+ 173.74
N.Y.S.E. Composite Index	140.98	− 1.08	+ 31.01
N.Y.S.E. Avg. Daily Vol. for Week (000's)	114,934	−26,971	− 5,516

* 46% Taxable equivalent 14.76%.

† Bond equivalent.

International Rates

	Friday 6/6/86	Week Ago
EURODOLLAR DEPOSIT RATES (bid)		
Overnight	6.75%	6.69%
1 month	7.00	7.00
3 month	7.00	7.00
6 month	7.06	7.06
1 year	7.25	7.25
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	8.67%	8.15%
Long Term (7 to 15 yrs.)	9.05	8.50

FOREIGN EXCHANGE SPOT RATES New York Opening (6/6/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02194	45.58
Canada	.7162	1.3963
Denmark	.1214	8.2400
France	.1406	7.1125
Germany	.4477	2.2335
Italy	.0006538	1529.50
Japan	.005942	168.30
Mexico	.001646	607.50
Netherlands	.3979	2.5130
Switzerland	.5432	1.8408
U.K.	1.5050	.6645

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The Manufacturers Hanover Financial Digest
Economic Commentary, Selected Financial Data, and Business Indicators

MONDAY, JUNE 23, 1986
VOLUME XXIII, NUMBER 14

Declining Energy Prices . . .

After five years of battling the worst economic crisis since the days of the Great Depression, American farmers are beginning to see scattered signs suggesting that the agricultural economy may be nearing the bottom of its slide. At long last, some relief from the deteriorating financial conditions that have battered so much of the U.S. agricultural sector seems to be in the offing. Lower oil prices and interest rates as well as declining fertilizer and land rental costs have reduced farm expenses and brightened profit potentials for financially healthy farmers.

The most important factor in the brighter outlook for American agriculture is the decline in farmers' costs of operation. Farmers' cash expenses dropped by an estimated $5 billion in 1985 and are expected to fall an additional $5 billion to $6 billion this year—the first time since the early 1930s that farmers' cash expenses have declined for two consecutive years.

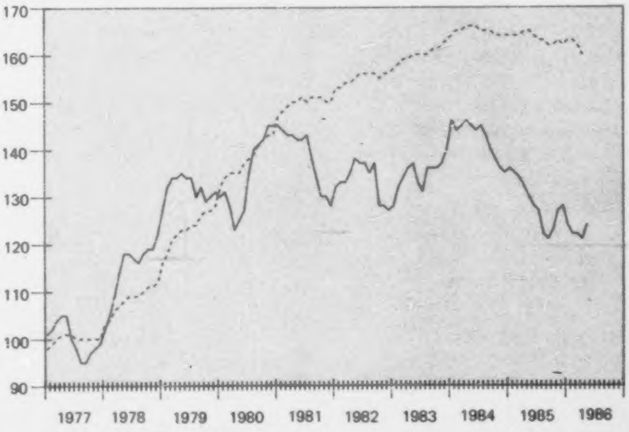
The drop in farmers' operating costs comes from three main sources: Lower energy prices and a related drop in such petroleum-based inputs as fertilizers, lower interest expenses resulting from lower interest rates and declining farm debt, and finally, a reduction in planted acreage due to wide participation of farmers in government programs with substantial set-aside requirements.

Lower fuel costs will have the largest impact on the reduction of farmers' expenses. From 1973 to 1981, energy costs as a percentage of total production outlays increased continuously, reaching a high of 6.3 percent in 1981. However, this year farmers' fuel bills may account for only four percent of their total expenses—the lowest share since 1974. In addition, the decline in fuel prices will also have broad secondary effects, cutting prices for related items such as fertilizers and pesticides.

. . . And Lower Interest Rates . . .

Interest expenses are also expected to decline significantly in 1986. These payments as a percentage of total production expenses more than doubled between 1970 and 1982. Since 1982, they have declined slightly, but a sharper drop is expected to take place this year. Total farm debt outstanding will likely register a small decline in 1986—the third drop in a row. Real estate debt should fall as farmers pay off old debts rather than acquire new land, while non-real estate debt will decline because the reductions in acres planted, input prices and capital expenditures lessen the need of external capital for many farmers.

INDEX OF PRICES RECEIVED BY FARMERS (LINE) VS.
INDEX OF PRICES PAID BY FARMERS (DOT) <1977=100>



Source: U.S. Department of Agriculture

Finally, farmers have already placed 3.8 million acres of their more erodible farmland into a long-term conservation reserve. Under a new five-year farm bill enacted last December, the U.S. Department of Agriculture will pay farmers to plant trees or grass on that land. The bill's goal is for farmers ultimately to place 40 million to 45 million acres, about ten percent of the nation's total farmland, in reserve by the end of 1990. Since farmers will plant fewer acres, they will need a smaller quantity of production inputs, thus spending fewer dollars to grow their 1986 crops. On the other hand, idle acreage will mean lost sales for chemical, seed, equipment, transportation and other businesses that supply farmers.

. . . Spell Some Relief For American Farmers

In addition to lower costs of production inputs, farm income will also be boosted by government

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farm program payments which could total a record $10 billion to $13 billion for 1986. Government payments could add up to nine percent of farmers' gross income this year, compared with approximately 4½ percent in 1985.

Notwithstanding these positive factors, net cash income, however, may not rise this year. This is because farmers' expenses are not falling in step with the prices they receive for their output. During the 12 months ending in April, farmers' costs of operation declined only 2½ percent, while farmgate prices dropped over eight percent, reaching one of the lowest levels since the end of 1978 (see chart on page 1). Bumper harvests of the past few years produced an oversupply of farm commodities, depressing their prices. Although fewer acres were planted this year, better-than-normal weather conditions are expected to produce another good harvest, pushing already bin-busting surpluses of farm commodities higher and prices lower.

As a result, farmers' crop receipts are expected to fall this year. This, of-course, will cut into farmers' gross income. Thus, lower farm costs and higher government payments will be offset by declining receipts for farmers' output. Not surprisingly, the U.S. Department of Agriculture now projects that farmers' net cash income in 1986 will just about

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending	$ Change Since	
Reserve Bank Credit	**6/18/86**	Week Ago	Year Ago
U.S. Gov'ts and Agencies Owned Outright & RPs	192.318	+ 2.370	+17.963
Loans to Depository Inst.	.734	+ .031	− .693
Float	1.067	+ .348	+ .269
Total Reserve Bank Credit	209.437	+ 3.091	+20.947
Treasury Deposits with Federal Reserve Banks	3.075	+ .600	+ .561
Currency in Circulation	198.880	+ .234	+13.240
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	148.407	+ 1.417	+26.006
Member Bank Reserves:	**6/18/86**		
Total Reserves Held	49.495	+ 1.635	+ 6.786
Excess (Deficiency)	.707	− .292	− .017
Net Free Reserves	.514	− .180	+ .301
		% Change Since	
Monetary Aggregates †		Three Months Ago*	Year Ago
M1 (6/9/86)	666.9	+ 18.1‡	+ 13.1‡
M2 (May '86)	2,647.0	+ 10.9	+ 8.0
M3 (May '86)	3,306.6	+ 8.3	+ 7.7
Domestic Nonfinancial Debt (1st Q'86)	7,033.5	+ 8.7	+ 14.2

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 6/20/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	6.26%	6.47%	6.60%
*** Federal Agencies**	6.49	6.63	6.76
*** Municipal Notes—High Grade (46% Taxable Equivalent)**	6.48	6.94	8.15
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
*** Secondary Market—Prime**	6.67	6.65	7.00

‡ Finance Company Paper—Prime		**‡* Bankers' Acceptances**	
5- 14 days	6.70%	Jul.	6.80%
15- 29 days	6.70	Aug.	6.75
30- 59 days	6.60	Sep.	6.65
60- 89 days	6.45	Oct.	6.60
90-179 days	6.25	Nov.	6.50
180-239 days	6.12	Dec.	6.45
240-270 days	6.12		

‡ Industrial Paper—Prime		**† Federal Funds Effective Rate**
30- 89 days	6.67%	
90-120 days	6.61	6.80%

‡ Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'86	$ 4,116r	$ 4,059	$ 3,918
Gross National Product (1982 Dollars)*	1st Q'86	$ 3,617r	$ 3,591	$ 3,548
Percent Change, Annual Rate	1st Q'86	2.9r	0.7	3.7
Change in Consumer Prices*	May '86n	2.4%	− 3.6%	2.4%
Change in Producer Prices*	May '86n	7.2%	− 7.2%	2.4%
Civilian Employment (Thousands of Persons) †	May '86	109,110	108,892	106,939
Unemployment as % of Civilian Labor Force †	May '86	7.3%	7.1%	7.3%
Personal Income*	May '86n	$ 3,445	$ 3,448r	$ 3,271
Leading Indicators Composite Index (1967=100) †	Apr '86	179.2	176.6	166.7
Industrial Production Index (1977=100) †	May '86n	124.2	125.0r	124.1
Net Change in Consumer Installment Credit †	Apr '86	$ 4.16	$ 3.09	$ 7.54
U.S. Merchandise Trade Balance †	Apr '86	−$ 12.07	−$ 12.18	−$ 12.11
Plant and Equipment Expenditures*	3rd Q'86n	$388.87(a)	$387.42(a)r	$388.90
Private Housing Starts (Thousands of Units)*	May '86n	1,888	2,039r	1,684
New Construction Expenditures*	Apr '86	$ 356.7	$ 353.9	$ 341.9
Total Business Inventories †	Apr '86n	$ 590.2	$ 588.2r	$ 578.5
Total Business Sales †	Apr '86n	$ 426.3	$ 420.2r	$ 423.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

match last year's levels—somewhere between $42 billion and $46 billion.

But while farmers will have more cash in their pockets, the overall financial picture of the farm sector could worsen slightly this year as deflation in farmland prices continues to erode the value of farmers' assets and net worth. The value of farmland, which accounts for the bulk of the total value of all farm assets, declined 12 percent in 1985, matching the previous year's fall—the largest since the Great Depression. This tumble marked the fifth consecutive year of falling prices for farmland. This year, however, the decline should be much smaller. Surveys in many parts of the nation's farm belt indicate that the decline in land values slowed in the first quarter, and many respondents felt that land values would stabilize in the second quarter.

To be sure, any recovery in the farm sector from the devastating slump of the recent years will be slow and uneven. It may not arrive soon enough for some of the farmers facing severe financial stress, asset liquidations, problems in obtaining credit and even bankruptcy. But the adjustments and changes in the farm sector, while hard and painful, are improving the financial conditions of farmers and slowly setting a stage for an improvement in the nation's important agricultural sector. H

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (6/4/86)	155,476	+ 44	– 62
New York City (6/11/86)	34,428	– 347	+ 1,418
Commercial Paper (6/11/86)	312,002	+ 195	+51,930

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (6/4/86)	259,627	+ 1,555	+ 4,099
New York City (6/11/86)	56,603	– 139	– 4,674

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (6/4/86)	738,060	+ 4,180	+ 57,309
New York City (6/11/86)	159,971	– 608	+ 8,853

Financial Markets

	Friday 6/20/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.25%	– .09	– .97
180-Day Bills†	6.43	– .09	– 1.14
Longest Bills†	6.57	– .07	– 1.33
Recent Issues:			
7s 6/30/88 (When Issued)	7.09	NA	
$7\frac{1}{4}$s 3/31/90	7.40	– .12	
$7\frac{3}{8}$s 5/15/96	7.60	– .14	
$7\frac{1}{4}$s 5/15/16	7.45	– .09	
Municipals:			
Bond Buyer–20 Bond Index* (6/19/86)	7.82%	– .26	– .87
Blue List Total ($ Million)	$1,850	–$ 247	– $ 244
30-Day Visible Supply ($ Million)	$3,060	–$1,410	+ $ 388
Total	$4,910	–$1,657	+ $ 144
Corporates:			
Moody's Aa Composite (6/19/86)	9.48%	– .12	– 1.87
30-Day Visible Supply ($ Million)	$3,845	+$ 25	+ $2,492
Stocks:			
Dow-Jones Averages:			
Industrials	1,879.54	+ 5.35	+ 555.39
Transportation	778.13	– 8.37	+ 128.55
Utilities	190.49	+ 2.80	+ 23.64
65 Stocks	717.61	+ .55	+ 171.17
N.Y.S.E. Composite Index	141.65	+ .65	+ 31.80
N.Y.S.E. Avg. Daily Vol. for Week (000's)	126,200	+ 888	+ 24,132

* 46% Taxable equivalent 14.48%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 6/20/86	Week Ago
Overnight	6.81%	6.81%
1 month	6.94	6.94
3 month	6.88	6.94
6 month	6.88	6.94
1 year	7.06	7.12
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.30%	8.04%
Long Term (7 to 15 yrs.)	7.77	8.19

FOREIGN EXCHANGE SPOT RATES

New York Opening (6/20/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02181	45.85
Canada	.7198	1.3893
Denmark	.1200	8.3300
France	.1397	7.1575
Germany	.4458	2.2430
Italy	.0006496	1539.50
Japan	.005968	167.55
Mexico	.001617	618.50
Netherlands	.3960	2.5255
Switzerland	.5419	1.8453
U.K.	1.5015	.6660

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The Manufacturers Hanover Financial Digest

Economic Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, JULY 7, 1986 VOLUME XXIII, NUMBER 15

Slack Business Conditions . . .

Despite expectations of a pronounced pickup in global business activity due to such positive economic developments as diminished rates of inflation, declining interest rates and reduced energy costs, the economies of several major industrial countries remain listless. A particular disappointment has been the economic performance of Japan and West Germany, both of which enjoy some of the world's lowest rates of inflation and interest, and were among the key beneficiaries of the plunge in oil prices.

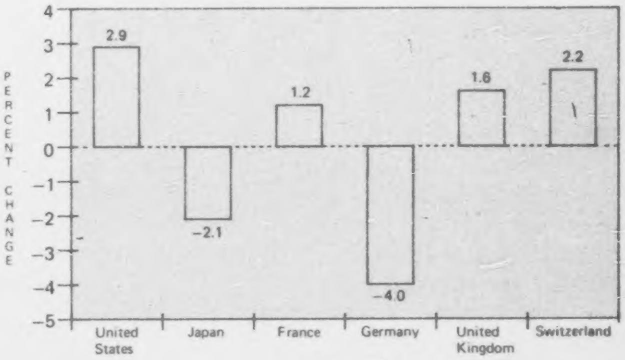
In the first quarter, however, each experienced a sizable drop in inflation-adjusted gross national product compared with quarter-earlier levels, with Germany's falling at a four percent annual rate and Japan's dropping at a 2.1 percent annual clip—the first quarter-over-quarter decline in Japanese real GNP since early 1975. What these developments have done, besides disappoint policymakers and economists alike, is again fuel expectations of another round of coordinated, industrial country interest rate reductions—a matter almost certain to be discussed at this week's Federal Open Market Committee meeting.

To be sure, the discussion will probably center on what went wrong, and what can be done about it. In Germany, for example, poor winter weather conditions negatively affected construction activity in the first quarter, while diminished domestic and foreign factory orders curbed industrial output. With respect to Japan, the strength of the yen has battered the economy, suppressing corporate profits, industrial production, investment activity and exports. In yen terms, overseas sales fell by nearly 14½ percent during the first five months of the year from their comparable 1985 levels. The decline in exports is a most significant development, as it was the external sector which had been the main prop of the economy in recent years. Domestic demand, in contrast, has remained weak. As in Germany, however, the Japanese government remains optimistic about future growth prospects—in sharp contrast to the gloomy assessment prevailing among private forecasters who predict a lackluster growth rate no higher than 2½ percent this year.

. . . Here And Abroad . . .

Elsewhere in the industrial world, the economic news is only slightly better, with export activity generally disappointing, investment activity weak and consumer spending soft. France's first quarter annualized growth rate, for instance, was a paltry 1.2 percent, the United Kingdom's was 1.6 percent, and Switzerland's was 2.2 percent (see chart). By comparison, the U.S. real GNP growth rate of 2.9 percent annualized would appear fairly satisfactory. However, several weak business statistics since then make it a good bet that economic growth slowed noticeably in the second quarter. What is more, the lackluster growth rates in the industrial world offer little confidence that the large number of unemployed will be reduced, particularly in Europe where double-digit rates prevail in several countries.

FIRST QUARTER 1986 REAL GNP GROWTH
IN SELECTED INDUSTRIAL COUNTRIES
(QUARTER-OVER-QUARTER AT ANNUAL RATES)



The sluggish economic performance in both the U.S. and overseas has sparked expectations that another round of coordinated interest rate cuts by the major industrial countries is imminent. Such expectations, in fact, have been fueling the rise of world stock markets in recent weeks with the U.S. and Japanese markets particularly buoyant. However, it is uncertain which country—the U.S., Germany or Japan—will lead the way. The Federal Reserve's policymakers, for example, may be somewhat reluctant to initiate another round of interest rate

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reductions because of rapid money growth as well as fears of precipitating a significant decline in the external value of the dollar.

What is more, with the trade deficit remaining large, the U.S. is eager for other nations to take the lead in stimulating economic activity, thus creating opportunities for hard-pressed U.S. exporters. The huge trade deficit has remained the Achilles heel of the economy, with the downward revision in first-quarter GNP due entirely to an increase in the originally estimated trade deficit. As a result, the U.S. Administration has been urging Germany and Japan to cut their interest rates in order to spur their domestic demand and thus encourage imports.

. . . Suggest Further Interest Rate Declines

Germany has hesitated to do so, however, because of the current weakness of the Deutschemark within the European Monetary System (EMS) and, as in the United States, above-target money supply growth. What is more, a snapback in retail sales, factory orders and industrial production during early spring has led some to suggest that further monetary stimulus is unnecessary. The Japanese also are wrestling with above-target money supply growth, and associated inflation rate fears. While this has not precluded previous discount rate cuts, there is a decided reluctance to move too far, too fast. However, the likelihood of continued economic sluggishness will probably tip the scales in favor of another round of discount rate cuts, with Japan

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 6/25/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	190.282	− 2.036	+ 15.270
Loans to Depository Inst.	.784	+ .050	+ .049
Float	.792	− .317	+ .478
Total Reserve Bank Credit	207.255	− 2.226	+ 19.203
Treasury Deposits with Federal Reserve Banks	3.428	+ .353	− .326
Currency in Circulation	198.429	− .439	+ 13.290
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	145.959	− 2.448	+ 24.200
	6/18/86		
Member Bank Reserves:			
Total Reserves Held	49.582	+ 1.744	+ 6.873
Excess (Deficiency)	.642	− .356	− .082
Net Free Reserves	.449	− .244	+ .236
Monetary Aggregates †		% Change Since Three Months Ago*	% Change Since Year Ago
M1 (6/23/86)	666.4	+ 18.3‡	+ 13.1‡
M2 (May '86)	2,646.9	+ 10.9	+ 7.9
M3 (May '86)	3,306.7	+ 8.3	+ 7.7
Domestic Nonfinancial Debt (1st Q'86)	7,033.5	+ 8.7	+ 14.2

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 7/3/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	5.94%	5.86%	5.91%
* Federal Agencies	6.23	6.13	6.08
* Municipal Notes—High Grade (46% Taxable Equivalent)	6.94	7.41	7.87
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.45	6.44	6.60

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	6.75%	Aug.	6.70%
15- 29 days	6.70	Sep.	6.50
30- 59 days	6.70	Oct.	6.40
60- 89 days	6.60	Nov.	6.33
90-179 days	6.55	Dec.	6.30
180-239 days	6.35	Jan.	6.30
240-270 days	6.35		

‡ Industrial Paper—Prime		† Federal Funds	
30- 89 days	6.70%		
90-120 days	6.55	Effective Rate	6.90%

‡ Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'86	$ 4,116	$ 4,059	$ 3,918
Gross National Product (1982 Dollars)*	1st Q'86	$ 3,617	$ 3,591	$ 3,548
Percent Change, Annual Rate	1st Q'86	2.9	0.7	3.7
Change in Consumer Prices*	May '86	2.4%	− 3.6%	2.4%
Change in Producer Prices*	May '86	7.2%	− 7.2%	2.4%
Civilian Employment (Thousands of Persons) †	Jun '86n	109,673	109,110	106,601
Unemployment as % of Civilian Labor Force †	Jun '86n	7.1%	7.3%	7.3%
Personal Income*	May '86	$ 3,445	$ 3,448	$ 3,271
Leading Indicators Composite Index (1967=100) †	May '86n	178.8	178.5r	167.1
Industrial Production Index (1977=100) †	May '86	124.2	125.0	124.1
Net Change in Consumer Installment Credit †	Apr '86	$ 4.16	$ 3.09	$ 7.54
U.S. Merchandise Trade Balance †	May '86n	−$ 14.21	−$ 14.28r	−$ 12.50
Plant and Equipment Expenditures*	3rd Q'86	$388.87(a)	$387.42(a)	$388.90
Private Housing Starts (Thousands of Units)*	May '86	1,888	2,039	1,684
New Construction Expenditures*	May '86n	$ 374.7	$ 371.6r	$ 352.0r
Total Business Inventories †	Apr '86	$ 590.2	$ 588.2	$ 578.5
Total Business Sales †	Apr '86	$ 426.3	$ 420.2	$ 423.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

most likely to lead the way after their July elections.

Whether or not further declines in interest rates in and of themselves will spark the economies of the industrial world is uncertain. Although nominal interest rates are already at their lowest level this decade, inflation-adjusted, or real interest rates remain at lofty heights. Still, Japan has reduced its discount rate from five percent at the end of last year to its present 3.5 percent, while in the U.S., the 30-year Treasury bond is at its lowest level since the late 1970s. In fact, one reason for the drop in interest rates, besides the collapse of inflationary expectations resulting from falling oil prices, is the ongoing weakness in the economies of the major countries.

A partial explanation for this lingering malaise lies with the stance of some governments' fiscal policies. With the notable exception of the United States, most governments have refused to adopt stimulative policies to reinforce the easing of their monetary policies, and have instead continued to pare their budget deficits. They apparently believe that the boost to real purchasing power arising from low inflation rates, low nominal interest rates, and falling oil prices will be sufficient to prompt faster growth. However, high real interest rates continue to retard business activity in general, and the energy price decline has so far produced more minuses than pluses in terms of output, employment and capital spending, suggesting that this could be another subdued year for the global economy—and that interest rates may move lower still.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since	
		Week Ago	Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (6/18/86)	154,364	– 724	– 1,488
New York City (6/18/86)	34,003	– 425	+ 1,309
Commercial Paper (6/18/86)	317,241	+ 5,233	+56,607

Bank Loans

(Millions of Dollars)

	Commercial and Industrial Loans		
	Latest Week	Change Since	
Weekly Reporting Large Commercial Banks		Week Ago	Year Ago
Nationwide (6/18/86)	258,908	– 277	+ 3,876
New York City (6/18/86)	56,251	– 352	– 4,994
	Total Loans and Leases Gross Adjusted		
	Latest Week	Change Since	
		Week Ago	Year Ago
Nationwide (6/18/86)	736,630	+ 1,262	+ 50,648
New York City (6/18/86)	159,195	– 43	+ 4,118

Financial Markets

	Thursday 7/3/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.05%	– .15	– .94
180-Day Bills†	6.08	– .19	– 1.04
Longest Bills†	6.24	– .20	– 1.13
Recent Issues:			
7s 6/30/88	6.64	– .19	
7¼s 3/31/90	7.02	– .13	
7⅜s 5/15/96	7.29	– .09	
7¼s 5/15/16	7.16	– .13	
Municipals:			
Bond Buyer–20 Bond Index* (7/2/86)	7.51%	– .08	– 1.31
Blue List Total ($ Million)	$1,874	–$ 165	– $ 29
30-Day Visible Supply ($ Million)	$4,408	+$1,360	+ $ 663
Total	$6,282	+$1,195	+ $ 634
Corporates:			
Moody's Aa Composite (7/1/86)	9.31%	– .04	– 2.15
30-Day Visible Supply ($ Million)	$3,725	+$ 820	+ $1,927
Stocks:			
Dow-Jones Averages:			
Industrials	1,900.87	+ 15.61	+ 565.18
Transportation	777.75	+ .25	+ 99.50
Utilities	200.76	+ 1.98	+ 34.42
65 Stocks	727.91	+ 4.63	+ 172.51
N.Y.S.E. Composite Index	144.67	+ 1.49	+ 33.03
N.Y.S.E. Avg. Daily Vol. for Week (000's)	135,278	+ 4,780	+ 45,688

* 46% Taxable equivalent 13.91%.

† Bond equivalent.

International Rates

	Thursday 7/3/86	Week Ago
EURODOLLAR DEPOSIT RATES (bid)		
Overnight	6.94%	6.88%
1 month	6.88	6.94
3 month	6.81	6.81
6 month	6.81	6.81
1 year	6.88	6.88
EURODOLLAR BONDS Average Yield		
Medium Term (5 to 7 yrs.)	7.67%	7.10%
Long Term (7 to 15 yrs.)	8.24	7.50

FOREIGN EXCHANGE SPOT RATES New York Opening (7/3/86)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.02251	44.43
Canada	.7257	1.3780
Denmark	.1240	8.0675
France	.1443	6.9300
Germany	.4607	2.1708
Italy	.0006709	1490.50
Japan	.006184	161.70
Mexico	.001552	644.50
Netherlands	.4089	2.4455
Switzerland	.5663	1.7660
U.K.	1.5460	.6468

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MANUFACTURERS HANOVER
Beverly Enterprises
$30,000,000
Senior Notes due 1993
MANUFACTURERS HANOVER
$26,000,000
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Economic Commentary, Selected Financial Data, and Business Indicators

MONDAY, JULY 21, 1986 VOLUME XXIII, NUMBER 16

Despite The Dollar's Drop . . .

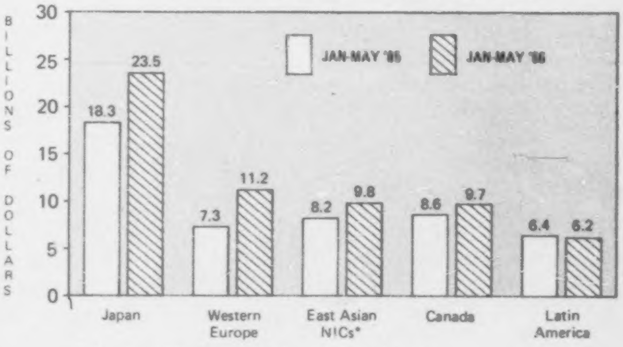
The sharp declines in interest rates, oil prices, and the dollar that occurred in 1985 and so far this year were widely expected to produce strong growth in the United States. However, with the second half of the year now underway, and the economy still moving sideways at best, growth forecasts are being scaled back. Even the Administration, among the most optimistic, predicting four percent annual growth in inflation-adjusted GNP this year, is expected to join in, lowering its growth forecast within the not-too-distant future. Thus, the question arises what went wrong and what can be done about it.

Perhaps the principal reason for today's lackluster growth pace is that a good chunk of consumer and business spending continues to be deflected abroad. The sharp decline in the dollar since February 1985 has failed to produce any noticeable improvement in U.S. trade performance. In fact, should current trends continue, this year's trade deficit will exceed 1985's record $148 billion figure. What is more, since total trade turnover (exports plus imports) currently represents some 15 percent of GNP versus only eight percent in 1970, the widening external deficit has become a substantial drain on U.S. economic performance.

To be sure, with the dollar slumping in the foreign exchange markets, this was not supposed to happen. But nearly a year and a half after the dollar began its almost nonstop decline against the other major industrial country currencies, the trade figures look as bad as ever, a reflection of the continued weakness in farm and manufactured exports, and the ongoing surge in imports. The U.S. trade deficit rose by over 25 percent in the first five months of this year from the same 1985 period, despite a better than 30 percent decline in the dollar against the currencies of Europe and Japan. Exports performed dismally, falling by almost four percent year-over-year, while imports rose by more than seven percent. In particular, foreign sales to Canada, Japan, Mexico and the United Kingdom all posted sizable declines.

Most recently, May's trade deficit of more than $14 billion did not come as a total surprise. The U.S. appetite for such foreign-produced products as autos, televisions and VCR's ensured that the manufactures deficit would remain large. What proved to be especially disappointing was the appearance of the first monthly farm-trade deficit since August 1971. Stepped-up purchases of produce from Mexico and higher-priced coffee from Brazil, along with diminished grain exports to the European Community and the Soviet Union, provided the one-two punch that put our farm trade in the red. The once-robust agricultural trade surplus, which peaked at nearly $27 billion in 1981, and once was the biggest single positive contributor to the U.S. trade balance, has virtually disappeared.

U.S. TRADE DEFICIT IN SELECTED AREAS: JANUARY-MAY 1986 VS. JANUARY-MAY 1985



*Includes Hong Kong, Singapore, South Korea and Taiwan

. . . The Trade Deficit Remains Huge . . .

One reason why the substantial currency realignments of the past year and a half have yet to prompt improved trade performance is that many European and Japanese companies have been shaving profit margins in an effort to maintain market share. They have not raised their prices nearly enough to reflect the rise in their currencies against the dollar. Take, for example, the automobile industry. Although the decline in the dollar against the yen to a new postwar low has obviously cut into the cost advantage that Japanese competitors enjoyed over American manufacturers, the Japanese have raised average prices by only 10 percent in the U.S., and even less in other markets. These increases have been insuffi-

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cient to diminish significantly Japanese auto sales in the U.S., where demand exceeds the 2.4 million Japanese vehicles that are allowed in each year under "voluntary" quotas. Moreover, quality, rather than price, may now be the most important factor in selling Japanese cars to Americans.

Another reason is that U.S. sales abroad have been hampered by the sluggish pace of overseas economic activity, prohibiting domestic exporters from reaping fully the cost advantages associated with the dollar's slide. Real GDP contracted in the first quarter in West Germany (down at a four percent annual rate, quarter-over-quarter) and Japan (down 2.1 percent, annualized), and barely inched forward in France and the United Kingdom.

Economic growth must occur abroad before U.S. exports can show healthy gains.

The restrained rise in import prices and slow growth overseas are not the only obstacles to a better trade performance. Often overlooked is the fact that the countries whose currencies have increased the most against the dollar are chiefly the other industrial countries, which now account for only half our overall trade deficit. But in addition to Western Europe and Japan, the U.S. trade deficit has widened rapidly with several other areas of the world this year—including Canada and the advanced developing countries of East Asia (see chart on page 1). The widening deficit with such countries as Canada, Korea and Taiwan stems

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 7/16/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	196.290	+ 1.755	+16.886
Loans to Depository Inst.	.824	+ .132	− .347
Float	.272	− .526	− .390
Total Reserve Bank Credit	213.455	+ 1.377	+19.860
Treasury Deposits with Federal Reserve Banks	3.992	+ .956	+ .773
Currency in Circulation	201.542	− .262	+13.485
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	151.275	− .749	+27.021
	7/16/86		
Member Bank Reserves:			
Total Reserves Held	50.775	+ 1.510	+ 7.368
Excess (Deficiency)	.599	− .688	− .091
Net Free Reserves	.283	− .650	+ .393

		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates†			
M1 (7/7/86)	673.9	+ 17.3‡	+ 12.8‡
M2 (June '86)	2,667.3	+ 11.7	+ 7.6
M3 (June '86)	3,326.9	+ 8.3	+ 7.4
Domestic Nonfinancial Debt (1st Q'86)	7,033.5	+ 8.7	+ 14.2

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 7/18/86	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	5.87%	6.03%	6.17%
* Federal Agencies	6.01	5.99	5.95
* Municipal Notes—High Grade (46% Taxable Equivalent)	7.41	7.78	8.33
Negotiable Time CDs			
Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.31	6.31	6.45

‡Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	6.30%	Aug.	6.35%
15- 29 days	6.32	Sep.	6.30
30- 59 days	6.27	Oct.	6.25
60- 89 days	6.25	Nov.	6.25
90-179 days	6.15	Dec.	6.20
180-239 days	6.00	Jan.	6.15
240-270 days	6.00		

‡Industrial Paper—Prime			
30- 89 days	6.28%	†Federal Funds	
90-120 days	6.20	Effective Rate	6.40%

‡ Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	1st Q'86	$ 4,116	$ 4,059	$ 3,918
Gross National Product (1982 Dollars)*	1st Q'86	$ 3,617	$ 3,591	$ 3,548
Percent Change, Annual Rate	1st Q'86	2.9	0.7	3.7
Change in Consumer Prices*	May '86	2.4%	− 3.6%	2.4%
Change in Producer Prices*	Jun '86n	0.0%	7.2%	− 2.4%
Civilian Employment (Thousands of Persons)†	Jun '86	109,673	109,110	106,601
Unemployment as % of Civilian Labor Force†	Jun '86	7.1%	7.3%	7.3%
Personal Income*	May '86	$ 3,445	$ 3,448	$ 3,271
Leading Indicators Composite Index (1967=100)†	May '86	178.8	178.5	167.1
Industrial Production Index (1977=100) †	Jun '86n	124.1	124.7r	124.3
Net Change in Consumer Installment Credit †	May '86n	$ 5.39	$ 4.30r	$ 6.33
U.S. Merchandise Trade Balance	May '86	−$ 14.21	−$ 14.28	−$ 12.50
Plant and Equipment Expenditures*	3rd Q'86	$388.87(a)	$387.42(a)	$388.90
Private Housing Starts (Thousands of Units)*	Jun '86n	1,845	1,860r	1,693
New Construction Expenditures*	May '86	$ 374.7	$ 371.6	$ 352.0
Total Business Inventories †	May '86n	$ 586.6	$ 588.6r	$ 577.8
Total Business Sales †	May '86n	$ 420.7	$ 428.5r	$ 424.4

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

from the fact that the dollar's well-publicized depreciation has not spilled over to the currencies of these countries.

. . . Suppressing Economic Growth

Indeed, some of the most intractable of our bilateral trade deficits are being experienced with the newly industrialized East Asian countries (NICs), particularly Taiwan, South Korea, Hong Kong and Singapore. These nations pursue an exchange rate policy of effectively tying their currencies to the U.S. dollar. The decline in the dollar, therefore, has fueled major trade gains for these countries in general, while at the same time, the substantial appreciation of the yen against the dollar has enhanced the export competitiveness of these NICs relative to Japan in particular. Not surprisingly, the U.S. deficit with the four East Asian NICs has widened, and now accounts for about one-sixth of the overall deficit. Nor has the deficit with Canada diminished; it accounts for another one-sixth.

When will this turn around? Not anytime soon, given the erosion of the farm trade surplus, the rapid growth of the trade deficit with the East Asian NICs and the ongoing external debt problems of many developing countries that have slashed their purchasing power. Even with further declines in the U.S. dollar, it is difficult to hope for any meaningful improvement in the U.S. trade deficit this year—a disappointing turn of events which will continue to suppress overall U.S. economic growth.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (7/2/86)	152,520	− 1,365	− 1,770
New York City (7/9/86)	133,192	− 297	+ 865
Commercial Paper (7/9/86)	314,271	+ 210	+50,530

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/2/86)	260,158	+ 351	+ 4,690
New York City (7/9/86)	56,056	− 955	− 4,274

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/2/86)	742,867	+ 7,248	+ 54,601
New York City (7/9/86)	160,270	− 854	+ 9,972

Financial Markets

	Friday 7/18/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	5.83%	− .05	− 1.55
180-Day Bills†	5.99	− .04	− 1.63
Longest Bills†	6.11	− .03	− 1.77
Recent Issues:			
7s 6/30/88	6.51	− .04	
7¼s 6/30/90	6.77	− .13	
7⅜s 5/15/96	7.16	− .12	
7¼s 5/15/16	7.20	+ .02	
Municipals:			
Bond Buyer–20 Bond Index* (7/17/86)	7.45%	−0−	− 1.28
Blue List Total ($ Million)	$2,142	+ $272	+ $ 324
30-Day Visible Supply ($ Million)	$6,572	+ $330	+ $3,119
Total	$8,714	+ $602	+ $3,443
Corporates:			
Moody's Aa Composite (7/17/86)	9.25%	+ .01	− 2.11
30-Day Visible Supply ($ Million)	$3,106	+ $605	− $ 247
Stocks:			
Dow-Jones Averages:			
Industrials	1,777.98	− 43.45	+ 418.44
Transportation	727.25	− 24.13	+ 26.52
Utilities	200.48	− 3.57	+ 34.24
65 Stocks	688.00	− 17.64	+ 121.92
N.Y.S.E. Composite Index	136.34	− 3.17	+ 23.05
N.Y.S.E. Avg. Daily Vol. for Week (000's)	150,166	+ 4,998	+ 21,524

* 46% Taxable equivalent 13.80%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 7/18/86	Week Ago
Overnight	6.31%	6.44%
1 month	6.50	6.56
3 month	6.50	6.56
6 month	6.50	6.56
1 year	6.56	6.62
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.53%	7.62%
Long Term (7 to 15 yrs.)	8.15	8.21

FOREIGN EXCHANGE SPOT RATES

New York Opening (7/18/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02252	44.41
Canada	.7257	1.3779
Denmark	.1241	8.0560
France	.1439	6.9490
Germany	.4649	2.1510
Italy	.0006770	1477.00
Japan	.006355	157.35
Mexico	.001610	621.00
Netherlands	.4125	2.4240
Switzerland	.5726	1.7465
U.K.	1.4955	.6687

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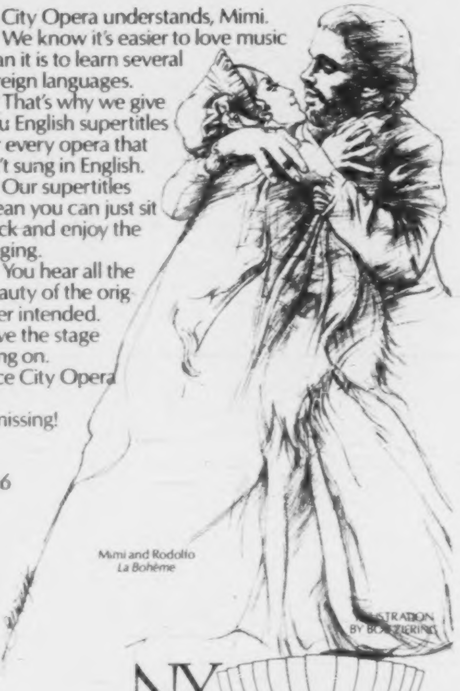

Mimi and Rodolfo
La Bohème

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• Candide—Bernstein (English)
Carmen—Bizet (French) (S)
• Cendrillon—Massenet (French) (S)
† Don Quichotte—Massenet (French) (S)
• Faust—Gounod (French) (S)
• Die Fledermaus—J. Strauss (English)
Kismet—Wright & Forrest (English)
The Love for Three Oranges—Prokofiev (French) (S)
Madama Butterfly—Puccini (Italian) (S)
• The Marriage of Figaro—Mozart (Italian) (S)
• Mefistofele—Boito (Italian) (S)
† The New Moon—Romberg (English)
Norma—Bellini (Italian) (S)
• The Pearl Fishers—Bizet (French) (S)
La Traviata—Verdi (Italian) (S)
† Werther—Massenet (French) (S)
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and Business Indicators

MONDAY, AUGUST 4, 1986
VOLUME XXIII, NUMBER 17

Although Real GNP Growth Slowed . . .

At first glance, the recent report on real gross national product (GNP) growth in the second quarter seems to point to a considerable slowdown in business activity. According to the Commerce Department, the nation's inflation-adjusted GNP expanded at an anemic 1.1 percent seasonally adjusted annual rate in the April-June period, not only well below the revised 3.8 percent growth rate posted in the first quarter, but also the slowest rate of rise since the final quarter of the 1981-82 recession. But, as is often the case, first appearances can be deceiving. A look beneath the surface of the top-line GNP number reveals an economy actually much stronger than it looks.

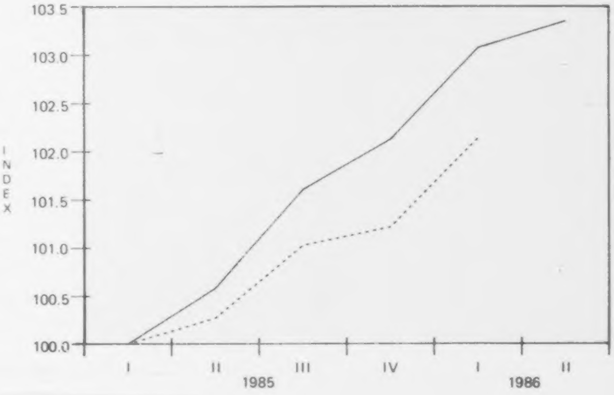
For one thing, the past performance of the economy was far better than many had thought. Upward revisions to real GNP in 1985 and the first quarter of 1986 boosted the level of output in the January-March period by more than $32 billion (see chart). For another, the slow growth pace of the second quarter reflected more changes in inventory spending and in the trade deficit, rather than any decided weakening of the economy. For when the effects of both a diminished pace of inventory accumulation, especially by auto retailers who were in the process of liquidating stocks, and the widening trade deficit are netted out of the GNP numbers, the pace of second quarter economic growth vaults from the reported 1.1 percent to a much healthier 5.5 percent annual rate.

This measure of economic activity—real final domestic demand, or real GNP minus net exports and the change in business inventories—reveals an economy which strengthened considerably in the second quarter, despite widespread perceptions to the contrary. Its annualized advance of 5.5 percent in the April-June period compares with a 1.9 percent decline in the first quarter—and is one and a half times the average rate of rise posted in the preceding five quarters. Consumer spending was the primary force driving this economic growth. Real consumption expenditures rose at a hefty 5.9 percent annual rate in the second quarter—the strongest gain in two years.

. . . A Look Beneath The Surface . . .

Despite this upturn in consumer spending, rising imports and a slower rate of inventory accumulation prevented strong domestic demand from being translated into healthy GNP growth last quarter. Although the value of the dollar has declined by more than 30 percent on a trade-weighted basis since February 1985, real imports soared more than 20 percent at an annual rate quarter-over-quarter, suggesting that the dollar's decline has yet to decrease significantly the proportion of U.S. demand being satisfied by foreign producers. Because of this deflection of a sizable chunk of domestic demand abroad, and an only modest three percent increase in exports, the inflation-adjusted net export deficit in the GNP accounts deteriorated by $20.4 billion in the second quarter compared with the first—a new record, which subtracted 2.2 percentage points from real growth. In other words, if the U.S. net export position in the second quarter had remained unchanged from the previous quarter, then GNP in the second quarter would have grown 3.3 percent.

REVISED REAL GNP (LINE)
VS. UNREVISED REAL GNP (DOT)
(FIRST QUARTER 1985=100)



While the growth-suppressing effects of the trade deficit were large, a reduction in the pace of inventory spending in the second quarter also was a major influence retarding GNP growth. The $19.6 billion increase in inflation-adjusted business inventories in

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the April-June period marked a significant deceleration in spending compared with the $40 billion accumulation pace of the previous quarter. Much of this reflected efforts of the auto retailers to work down hefty stocks of cars which had piled up prior to the latest round of dealer-financing incentives. This slowdown in inventory spending reduced the level of real GNP in the second quarter by more than $20 billion, subtracting 2.2 percentage points from the second quarter's growth rate.

. . . Reveals A Stronger Economy

These changes in inventory spending and net exports, and their significant effects on output, can be seen by comparing the economic trends of last quarter with those of the first, when real GNP posted a 3.8 percent annual rate of gain. Output growth in the first was boosted by the narrowing of the net export deficit and a substantial rise in the rate of inventory accumulation. Therefore, when the GNP-boosting effect of the hefty, and largely involuntary, buildup in inventories and improvements in our net export position are netted out, a somewhat different picture emerges for the January-March period: The first quarterly drop in inflation-adjusted final domestic demand since the onset of the current business expansion at the end of 1982.

Although the second quarter's GNP growth rate tended to mask the strength of final sales, and

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 7/30/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	192.383	– .534	+17.467
Loans to Depository Inst.	.746	+ .088	– .204
Float	.608	+ .223	– .012
Total Reserve Bank Credit	209.795	+ .500	+20.619
Treasury Deposits with Federal Reserve Banks	3.862	+ .229	+ .137
Currency in Circulation	199.655	– .804	+13.095
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	151.639	– .053	+25.996
	7/30/86		
Member Bank Reserves:			
Total Reserves Held	49.953	– .894	+ 7.529
Excess (Deficiency)	1.182	+ .484	+ .229
Net Free Reserves	.774	+ .392	+ .232
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates †			
M1 (7/21/86)	677.7	+ 18.5‡	+ 13.1‡
M2 (June '86)	2,668.9	+ 12.0	+ 7.7
M3 (June '86)	3,322.5	+ 7.6	+ 7.3
Domestic Nonfinancial Debt (1st Q'86)	7,033.5	+ 8.7	+ 14.2

†Seasonally adjusted.

* Seasonally adjusted annual rate.

‡ Four-week moving average.

New York Money Market

Offering Rates 8/1/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	5.76%	5.76%	5.77%
* Federal Agencies	6.04	5.94	5.93
* Municipal Notes—High Grade (46% Taxable Equivalent)	8.15	8.33	8.89
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.23	6.23	6.30

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	6.28%	Sep.	6.16%
15- 29 days	6.28	Oct.	6.13
30- 59 days	6.28	Nov.	6.10
60- 89 days	6.23	Dec.	6.08
90-179 days	6.15	Jan.	6.05
180-239 days	6.00	Feb.	6.03
240-270 days	6.00		

‡ Industrial Paper—Prime			
30- 89 days	6.22%	†Federal Funds	
90-120 days	6.14	Effective Rate	6.35%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	2nd Q'86n	$ 4,182	$ 4,149r	$ 3,965r
Gross National Product (1982 Dollars)*	2nd Q'86n	$ 3,666	$ 3,656r	$ 3,568r
Percent Change, Annual Rate	2nd Q'86n	1.1	3.8r	2.3r
Change in Consumer Prices*	Jun '86n	6.0%	2.4%	2.4%
Change in Producer Prices*	Jun '86	0.0%	7.2%	– 2.4%
Civilian Employment (Thousands of Persons) †	Jul '86n	109,882	109,673	106,871
Unemployment as % of Civilian Labor Force †	Jul '86n	6.9%	7.1%	7.3%
Personal Income*	Jun '86n	$ 3,479	$ 3,476r	$ 3,305r
Leading Indicators Composite Index (1967=100) †	Jun '86n	178.6	178.1r	167.7
Industrial Production Index (1977=100) †	Jun '86	124.1	124.7	124.3
Net Change in Consumer Installment Credit †	May '86	$ 5.39	$ 4.30	$ 6.33
U.S. Merchandise Trade Balance	Jun '86n	–$ 14.17	–$ 13.12r	–$ 10.50
Plant and Equipment Expenditures*	3rd Q'86	$388.87(a)	$387.42(a)	$388.90
Private Housing Starts (Thousands of Units)*	Jun '86	1,845	1,860	1,693
New Construction Expenditures*	Jun '86n	$ 375.1	$ 374.9r	$ 352.9
Total Business Inventories †	May '86	$ 586.6	$ 588.6	$ 577.8
Total Business Sales †	May '86	$ 420.7	$ 428.5	$ 424.4

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

especially consumer spending, one does not have to look far to find soft spots in business activity. The continued leakage of domestic demand abroad is hurting the goods-producing sector, and the plunge in energy prices is putting the squeeze on the oil and gas industry. As a result, industrial production has declined four times in the past five months and is no higher now than its level a year ago. Reduced production, in turn, has led to layoffs in manufacturing industries which have lost almost 160,000 jobs since the beginning of this year alone.

This burden has caused a sharp division in employment patterns between those sectors which produce goods and those which provide services. While the manufacturing sector has failed to make up for the jobs lost in the last recession, service-providing industries, which are barely affected by import competition, are thriving. This dichotomy fits the general pattern of an economy split between a strong consumption side and a weak production side. Nor is it expected to change any time soon. While the workdown of inventories could set the stage for a modest snapback in production in the current and in subsequent quarters, no major reduction appears likely in the growth-inhibiting effects of the trade deficit until the dollar weakens further and economic activity picks up abroad (Financial Digest—July 21, 1986).

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (7/16/86)	152,302	+ 566	– 944
New York City (7/23/86)	33,463	– 448	+ 787
Commercial Paper (7/23/86)	315,363	– 1,342	+50,554

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/16/86)	257,504	– 1,469	+ 3,090
New York City (7/23/86)	55,550	– 490	– 4,088

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/16/86)	740,155	– 610	+ 53,956
New York City (7/23/86)	157,281	– 2,582	+ 11,073

Financial Markets

	Friday 8/1/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	5.91%	– .03	– 1.62
180-Day Bills†	6.00	– .10	– 1.88
Longest Bills†	6.11	– .14	– 2.11
Recent Issues:			
$6\frac{5}{8}$s 7/31/86	6.52	– .12	
$7\frac{1}{4}$s 6/30/90	6.91	– .11	
$7\frac{3}{8}$s 5/15/96	7.33	– .01	
$7\frac{1}{4}$s 5/15/16	7.46	+ .06	
Municipals:			
Bond Buyer–20 Bond Index* (7/31/86)	7.54%	– .06	– 1.47
Blue List Total ($ Million)	$2,276	–$ 116	+ $ 186
30-Day Visible Supply ($ Million)	$4,653	–$1,368	+ $1,705
Total	$6,929	–$1,484	+ $1,891
Corporates:			
Moody's Aa Composite (7/31/86)	9.31%	– .02	– 2.22
30-Day Visible Supply ($ Million)	$3,550	+$ 260	+ $ 97
Stocks:			
Dow-Jones Averages:			
Industrials	1,763.64	– 46.40	+ 410.59
Transportation	713.00	– 7.50	+ 13.56
Utilities	203.28	– 4.17	+ 46.43
65 Stocks	682.86	– 1.45	+ 123.46
N.Y.S.E. Composite Index	135.29	– 3.12	+ 24.44
N.Y.S.E. Avg. Daily Vol. for Week (000's)	123,630	– 5,309	+ 17,102

* 46% Taxable equivalent 13.96%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 8/1/86	Week Ago
Overnight	6.31%	6.25%
1 month	6.38	6.50
3 month	6.38	6.50
6 month	6.38	6.50
1 year	6.44	6.63
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.67%	7.64%
Long Term (7 to 15 yrs.)	8.24	8.21

FOREIGN EXCHANGE SPOT RATES

New York Opening (8/1/86)	U.S. $ Equivalent	Currency Per U.S. $
Belgium	.02320	43.10
Canada	.7245	1.3803
Denmark	1268	7.8865
France	.1474	6.7825
Germany	.4791	2.0872
Italy	.0006976	1433.55
Japan	.006498	153.90
Mexico	.001550	645.00
Netherlands	.4244	2.3560
Switzerland	.5988	1.6700
U.K.	1.4899	.6712

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VOLUME XXIII, NUMBER 18

With The Consumer At The Throttle . . .

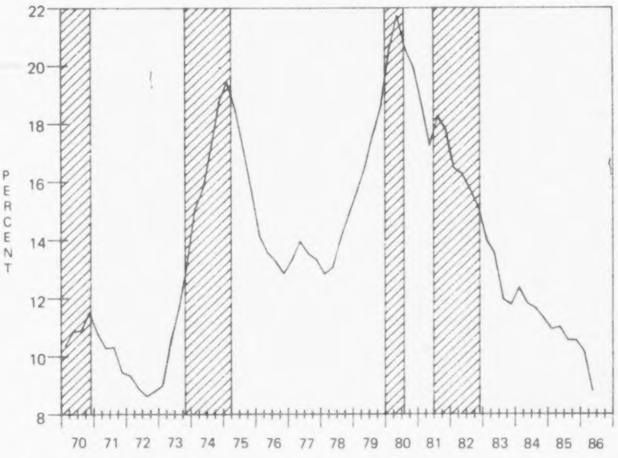
The scant 0.1 percent increase in retail sales during July, coupled with the downward revision in June's figure, has once again raised questions about the ability of the consumer sector to keep the economy expanding for the rest of this year and into 1987. For even more than usual, the U.S. economy is being driven by consumer spending. During the first half of 1986, real personal consumption accounted for nearly all of the $58 billion increase in real domestic demand (real GNP less net exports). In the second quarter of 1986, real consumer spending bolted upward at close to a six percent seasonally adjusted annual rate, compared with the anemic 1.1 percent rise in the overall economy. However, recent statistics that suggest weakness in retail sales as well as in housing and incomes, plus the continuing decline of manufacturing and mining employment, have economists asking: Can the consumer keep spending?

A look at employment, incomes and inflation, probably the best gauges of consumer economic well-being, would seem to justify expectations that the consumer sector can—and will—continue to increase spending over the next few quarters. The unemployment rate returned to 6.9 percent in July, and the employment rate—the percentage of the adult population with jobs—now stands at a record 60.8 percent. Total employment crossed the 111.5-million-worker mark for the first time ever in July, paced by job increases in service-producing industries and construction.

Overall personal income growth did soften in May and June, but this weakness was caused by two nonrecurring events: a drop-off in subsidy payments to farmers and a strike by communications workers. Excluding these two factors, personal incomes during May and June would have increased by $24.5 billion instead of falling by nearly $6 billion.

More good news comes from the inflation front. Consumer prices were down during the first six months of 1986, enabling consumers to enjoy increased buying power from their take-home pay. Because of this, the discomfort index—the unemployment rate plus the inflation rate—plummeted also. In the second quarter of 1986, it averaged 8.81 percent—the lowest level in almost 14 years (see chart).

DISCOMFORT INDEX:
SUM OF UNEMPLOYMENT AND INFLATION RATES



. . . The Expansion Remains On Track . . .

Households are also improving their financial positions. Financial assets during the fourth quarter of 1985 and the first quarter of 1986 grew at a seasonally adjusted annual rate of 23.5 percent, due mainly to a rapid buildup of mutual fund deposits. Household liabilities, on the other hand, rose only at an 11.5 percent annual rate during this same period, as consumers began to rein in their use of credit, a trend that is still continuing. In the first half of 1986, consumers took on only $32.2 billion in installment credit—the smallest six-month increase in three years.

June's rise in consumer credit was a modest $5.1 billion—due mainly to growth in automobile credit which was enhanced by financing incentives. Credit extended by retailers decreased during the month, and the fall in gasoline prices caused credit outstanding at gasoline companies to drop $109 million. By better managing their funds, consumers have vastly improved their balance sheets. According to

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the Federal Reserve, households now hold $3.26 in financial assets for every $1 of liabilities, the highest such ratio since 1976.

One factor that heightened worries about a consumer-spending slowdown was the drop in housing starts in May and June. Since housing construction is considered a prime catalyst for the economy, concerns arose that this sector was beginning a downturn that could affect other areas of business. However, despite the two consecutive monthly drops, starts for the first half of 1986 are still running 11.5 percent above the comparable period of last year. Moreover, sales of new single-family homes for the first six months of 1986 are 18 percent above last year's January-June period, and the percent of families surveyed who are planning to buy a new home within the next six months is still strong. Both the national median sales price and the mortgage rate for a new home decreased in June. This raised the proportion of families who can afford to purchase a new home to 37 percent from only 23 percent two years ago.

. . . As Long As Imports Don't Derail It

Certainly, there are some signs that all is not perfect in the consumer sector. For one thing, the economy is not growing evenly across the U.S. For example, West Virginia and Mississippi have battled high unemployment during this expansion. The severe problems of the energy sector have boosted

Selected Federal Reserve Data

(Averages of Daily Figures--Billions of Dollars)

Reserve Bank Credit	Week Ending 8/13/86	$ Change Since Week Ago	$ Change Since Year Ago
U.S. Gov'ts and Agencies Owned Outright & RPs	193.407	+ .550	+16.802
Loans to Depository Inst.	.812	+ .107	− .332
Float	.402	− .907	− .170
Total Reserve Bank Credit	211.366	+ .039	+19.827
Treasury Deposits with Federal Reserve Banks	3.695	+ .171	+ .663
Currency in Circulation	201.386	+ .779	+13.049
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	155.491	+ 1.597	+31.054
Member Bank Reserves:	8/13/86		
Total Reserves Held	50.470	+ .531	+ 7.322
Excess (Deficiency)	.589	− .518	− .149
Net Free Reserves	.203	− .496	− .054

Monetary Aggregates †		% Change Since Three Months Ago*	% Change Since Year Ago
M1 (8/4/86)	679.6	+ 18.2‡	+ 13.3‡
M2 (July '86)	2,697.1	+ 11.6	+ 8.1
M3 (July '86)	3,358.5	+ 8.4	+ 7.9
Domestic Nonfinancial Debt (1st Q'86)	7,033.5	+ 8.7	+ 14.2

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 8/15/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	5.56%	5.53%	5.62%
* Federal Agencies	5.73	5.70	5.72
* Municipal Notes—High Grade (46% Taxable Equivalent)	7.87	8.33	8.80
Negotiable Time CDs Manufacturers Hanover		Rates By Arrangement	
* Secondary Market—Prime	5.98	5.95	6.10

‡ Finance Company Paper—Prime	
5- 14 days	6.13%
15- 29 days	6.13
30- 59 days	6.10
60- 89 days	6.02
90-179 days	5.88
180-239 days	5.75
240-270 days	5.75

‡* Bankers' Acceptances	
Sep.	6.12%
Oct.	6.00
Nov.	5.90
Dec.	5.81
Jan.	5.78
Feb.	5.74

‡ Industrial Paper—Prime	
30- 89 days	6.08%
90-120 days	5.98

† Federal Funds Effective Rate 6.40%

‡ Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	2nd Q'86	$ 4,182	$ 4,149	$ 3,965
Gross National Product (1982 Dollars)*	2nd Q'86	$ 3,666	$ 3,656	$ 3,568
Percent Change, Annual Rate	2nd Q'86	1.1	3.8	2.3
Change in Consumer Prices*	Jun '86	6.0%	2.4%	2.4%
Change in Producer Prices*	Jul '86n	− 4.8%	0.0%	2.4%
Civilian Employment (Thousands of Persons) †	Jul '86	109,882	109,673	106,871
Unemployment as % of Civilian Labor Force†	Jul '86	6.9%	7.1%	7.3%
Personal Income*	Jul '86	$ 3,479	$ 3,476	$ 3,305
Leading Indicators Composite Index (1967=100)†	Jun '86	178.6	178.1	167.7
Industrial Production Index (1977=100) †	Jul '86n	124.1	124.2r	124.1
Net Change in Consumer Installment Credit †	Jun '86n	$ 5.07	$ 6.46r	$ 4.39
U.S. Merchandise Trade Balance	Jun '86	−$ 14.17	−$ 13.12	−$ 10.50
Plant and Equipment Expenditures*	3rd Q'86	$388.87(a)	$387.42(a)	$388.90
Private Housing Starts (Thousands of Units)*	Jun '86	1,845	1,860	1,693
New Construction Expenditures*	Jun '86	$ 375.1	$ 374.9	$ 352.9
Total Business Inventories †	Jun '86n	$ 589.0	$ 586.7r	$ 580.1
Total Business Sales †	Jun '86n	$ 423.6	$ 421.6r	$ 418.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

unemployment rates in Louisiana and Alaska to double-digit levels. The heat wave and drought in the Southeast continue to destroy crops, poultry and livestock in that region. For another, despite the slowdown in debt accumulation, consumer credit outstanding remains at record levels both in absolute terms and as a percent of disposable income. And the uncertainty of tax reform has postponed certain consumer buying decisions, especially in housing and other credit-related purchases.

On the whole, however, concerns should not center on whether U.S. consumers will continue to spend. The average consumer is still able to increase his or her expenditures. The more important worry is from what source this demand will be satisfied. As long as the nation's trade deficit remains large, increased consumer spending will not necessarily translate into a more robust rate of output for the U.S. economy. Indeed, the $20.4 billion increase in the real net export deficit used to determine real GNP during the second quarter of 1986 subtracted more than two percentage points from the nation's overall growth rate. And although consumers increased their nominal-dollar purchases of durable goods by 5.8 percent in the second quarter of 1986 compared to the second quarter of 1985, output of consumer hardgoods by U.S. factories rose only 2.3 percent in the same period. This gap between demand and production was satisfied by a 17.3 percent surge in U.S. imports of consumer durable goods.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (7/30/86)	153,430	+ 188	– 317
New York City (8/6/86)	33,480	+ 154	+ 754
Commercial Paper (8/6/86)	318,128	+ 2,876	+48,815

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/30/86)	256,799	+ 20	+ 1,594
New York City (8/6/86)	56,572	+ 812	– 3,636

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/30/86)	736,321	+ 719	+ 50,209
New York City (8/6/86)	157,934	– 215	+ 9,585

Financial Markets

	Friday 8/15/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	5.70%	– .13	– 1.64
180-Day Bills†	5.76	– .22	– 1.89
Longest Bills†	5.93	– .14	– 2.03
Recent Issues:			
$6^{5}/_{8}$s 7/31/88	6.31	– .18	
$7^{1}/_{4}$s 6/15/90	6.67	– .18	
$7^{3}/_{8}$s 5/15/96	7.13	– .16	
$7^{1}/_{4}$s 5/15/16	7.28	– .13	
Municipals:			
Bond Buyer–20 Bond Index* (8/14/86)	7.33%	– .20	– 1.79
Blue List Total ($ Million)	$2,268	–$ 95	+ $ 277
30-Day Visible Supply ($ Million)	$3,182	–$1,571	– $1,327
Total	$5,450	–$1,666	– $1,050
Corporates:			
Moody's Aa Composite (8/14/86)	9.23%	– .10	– 2.26
30-Day Visible Supply ($ Million)	$2,221	–$ 824	+ $ 613
Stocks:			
Dow-Jones Averages:			
Industrials	1,855.60	+ 72.98	+ 542.88
Transportation	756.00	+ 43.12	+ 89.22
Utilities	211.24	+ 7.24	+ 54.03
65 Stocks	718.42	+ 30.98	+ 175.76
N.Y.S.E. Composite Index	142.22	+ 5.81	+ 34.30
N.Y.S.E. Avg. Daily Vol. for Week (000's)	132,330	+ 4,464	+ 48,664

* 46% Taxable equivalent 13.57%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 8/15/86	Week Ago
Overnight	6.31%	6.31%
1 month	6.19	6.38
3 month	6.06	6.31
6 month	6.06	6.31
1 year	6.12	6.44
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.46%	7.62%
Long Term (7 to 15 yrs.)	8.06	8.15

FOREIGN EXCHANGE SPOT RATES

New York Opening (8/15/86)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.02336	42.80
Canada	.7196	1.3896
Denmark	.1285	7.7825
France	.1489	6.7175
Germany	.4839	2.0665
Italy	.0007030	1422.50
Japan	.006487	154.15
Mexico	.001476	677.50
Netherlands	.4296	2.3280
Switzerland	.6008	1.6645
U.K.	1.4950	.6689

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The Manufacturers Hanover Financial Digest

Economic Commentary,
Selected Financial Data,
and Business Indicators

FRIDAY, AUGUST 29, 1986

VOLUME XXIII, NUMBER 19

Correcting The Trade Deficit . . .

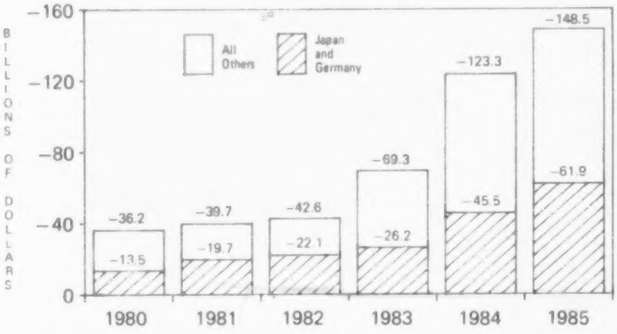
The sizable imbalances in the external account positions of the three largest industrial nations, the United States, Japan and Germany, are now viewed as one of the more serious problems facing the world economy. While the U.S. has seen its trade deficit soar well into 12-digit territory, the Japanese and Germans have experienced the opposite: namely, marked increases in their surpluses. One response to this problem has been a year-long effort by the United States to guide the dollar lower in the foreign exchange markets. Another, of more recent vintage, has been a rising chorus of calls for faster economic growth in Japan and Germany—presumably enhancing U.S. export opportunities and trimming substantially the overall red-ink total.

While this approach appears to have a good deal of merit, a word of caution is in order. The U.S. trade deficit is now too large, and the proportion of U.S. exports absorbed by these countries is too small, for faster growth in Japan and Germany alone to cure what ails the trade balance. Only by diminishing further the price attractiveness of imports, while enhancing that of exports, will more significant near-term improvements occur—a remedy requiring an even weaker dollar in the foreign exchange markets.

The U.S. Administration had hoped that the better than 30 percent decline in the trade-weighted value of the dollar from its peak of February 1985 would help to narrow our trade deficit. This has not yet happened. In fact, the U.S. deficit has gotten worse and is expected to exceed last year's record shortfall of $148.5 billion by at least ten percent. This development has led the Administration to seek another avenue in finding a solution to the widening trade deficit.

By urging Japan and Germany to adopt more stimulative fiscal and monetary policies, the hope is that the resulting faster growth will prompt stepped-up demand for U.S.-produced goods. In this regard, Japan's bilateral surplus is of particular concern; exports to the United States rose from three percent to nearly five percent of Japanese GNP between 1980 and 1985, and its surplus with this country is expected to approach $60 billion this year, almost three times the $21.7 billion surplus it ran with the U.S. in 1983. The trade deficit with Germany, although far smaller, still totaled a shade more than $12 billion last year, and could hit $15 billion this year. Together they now account for better than 40 percent of the global U.S. trade deficit (see chart).

U.S. TRADE DEFICIT:
GLOBAL AND WITH JAPAN AND GERMANY
(Exports f.a.s./Imports c.i.f.)



. . . Requires More Than Faster Growth . . .

Japan's and Germany's growing trade surpluses and low rates of inflation would seem to give them quite a bit of leeway to stimulate their domestic economies. In fact, on the surface, the emergence of such large surpluses might indicate that domestic demand is relatively weak. In the case of Germany, for example, inflation-adjusted domestic demand was not much larger in 1985 than it was in 1981, expanding at an anemic 0.1 percent average annual rate during the period. But, so far, both countries have shown great reluctance to heed U.S. advice. Japanese and German officials continue to insist that falling oil prices, low inflation and declining interest rates will boost domestic demand all by themselves. However, even if Japan and Germany did grow rapidly, the favorable impact on the U.S. trade deficit may be limited.

Take, for example, Japan, which now accounts for some 12 percent of U.S. exports. Exports to that country have been growing at an average annual rate of about five percent since the beginning of the decade, and totaled $22½ billion last year. Thus, even if the rate of export growth was to double in

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coming years—reaching double-digit territory—it would add no more than $2½ billion to the present level of U.S. export sales in the first year, and an additional $13 billion to exports by the fifth year. To be sure, while $13 billion is not an insignificant sum, if imports remained unchanged, it would trim today's bilateral trade deficit by only one-fifth by the early 1990s.

So, too, in the case of Germany, which accounts for an even smaller proportion of global U.S. exports. It purchased four percent, or $9 billion of U.S. goods in 1985. For one thing, even at its high point, Germany never absorbed more than five percent of total U.S. exports. This was in 1980, just about the last time that Germany was attempting to act as a locomotive for Europe's growth. If this peak proportion prevailed today, it would add only $2 billion to U.S. exports, trimming the bilateral deficit with Germany by some 15 percent.

. . . In Japan And Germany Alone

For another, although U.S. exports to Germany are 17 percent below their 1980 peak, a good chunk of this decline—about a quarter—was accounted for by a dip in shipments of agricultural commodities. While faster growth in Germany may bolster demand for U.S. manufactured goods, it is questionable that it would lead to similar increases in sales of such commodities as tobacco and soybeans. However, even if it did, perhaps more important is this: Had U.S. exports increased by 17 percent since

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 8/27/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	193.642	+ .557	+16.935
Loans to Depository Inst.	.887	− .046	− .209
Float	.752	+ .303	+ .604
Total Reserve Bank Credit	210.711	+ .749	+20.824
Treasury Deposits with Federal Reserve Banks	3.284	− .170	+ .848
Currency in Circulation	200.612	− .672	+13.367
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	155.291	− .814	+31.232
	8/27/86		
Member Bank Reserves:			
Total Reserves Held	50.491	− .016	+ 7.613
Excess (Deficiency)	.790	+ .208	− .160
Net Free Reserves	.395	+ .199	− .077

Monetary Aggregates†		% Change Since Three Months Ago*	% Change Since Year Ago
M1 (8/18/86)	688.1	+ 17.1‡	+ 13.3‡
M2 (July '86)	2,698.5	+ 11.6	+ 8.1
M3 (July '86)	3,371.5	+ 9.5	+ 8.3
Domestic Nonfinancial Debt (1st Q'86)	7,033.5	+ 8.7	+ 14.2

†Seasonally adjusted.

* Seasonally adjusted annual rate.

‡ Four-week moving average.

New York Money Market

Offering Rates 8/29/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	5.18%	5.18%	5.24%
* Federal Agencies	5.29	5.28	5.28
* Municipal Notes—High Grade (46% Taxable Equivalent)	6.94	7.87	8.15
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	5.45	5.45	5.55

‡ Finance Company Paper—Prime	
5- 14 days	5.40%
15- 29 days	5.40
30- 59 days	5.35
60- 89 days	5.30
90-179 days	5.30
180-239 days	5.25
240-270 days	5.25

‡* Bankers' Acceptances	
Sep.	5.52%
Oct.	5.42
Nov.	5.40
Dec.	5.36
Jan.	5.33
Feb.	5.30

‡ Industrial Paper—Prime	
30- 89 days	5.39%
90-120 days	5.32

† Federal Funds Effective Rate 5.75%

‡ Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	2nd Q'86	$ 4,180r	$ 4,149	$ 3,965
Gross National Product (1982 Dollars)*	2nd Q'86	$ 3,662r	$ 3,656	$ 3,568
Percent Change, Annual Rate	2nd Q'86	0.6r	3.8	2.3
Change in Consumer Prices*	Jul '86n	0.0%	6.0%	2.4%
Change in Producer Prices*	Jul '86	− 4.8%	0.0%	2.4%
Civilian Employment (Thousands of Persons)†	Jul '86	109,882	109,673	106,871
Unemployment as % of Civilian Labor Force†	Jul '86	6.9%	7.1%	7.3%
Personal Income*	Jul '86n	$ 3,502	$ 3,487r	$ 3,315
Leading Indicators Composite Index (1967=100)†	Jul '86n	179.4	177.4r	169.2
Industrial Production Index (1977=100) †	Jul '86	124.1	124.2	124.1
Net Change in Consumer Installment Credit †	Jun '86	$ 5.07	$ 6.46	$ 4.39
U.S. Merchandise Trade Balance	Jul '86n	−$ 18.04	−$ 13.25	−$ 13.58
Plant and Equipment Expenditures*	3rd Q'86	$388.87(a)	$387.42(a)	$388.90
Private Housing Starts (Thousands of Units)*	Jul '86n	1,818	1,852r	1,673
New Construction Expenditures*	Jun '86	$ 375.1	$ 374.9	$ 352.9
Total Business Inventories †	Jun '86	$ 589.0	$ 586.7	$ 580.1
Total Business Sales †	Jun '86	$ 423.6	$ 421.6	$ 418.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

1980, rather than decreased by this amount, the results would not be all that much different—sales to Germany would be some $4 billion greater, and the global trade deficit a paltry 2½ percent smaller.

On the import side, in contrast, the American appetite for foreign products has not abated despite the fall in the value of the dollar. In many cases, Japanese and German competitors have held onto market share by cutting into profit margins. In other instances, there is little or no domestic competition as in the case of German luxury cars and Japanese electronic products. Finally, the dependability, reliability and quality of these products are key selling points. Thus, even under the most optimistic of circumstances, more rapid growth in Japan and Germany alone will not significantly reduce our bilateral deficits with these nations—given the hefty U.S. appetite for their products, and the limited potential for expanding exports to them quickly.

This means that additional exchange rate changes may be necessary if the trade deficit is to stabilize, and then narrow. While further dollar depreciation is no panacea by itself, it will certainly diminish the attractiveness of imports, giving longer-run solutions time to work. For over time, stronger growth in Japan and Germany, the lowering of additional barriers worldwide to market entry, and a further receding of the liquidity problems of Latin America will create a favorable climate for U.S. exporters to take full advantage of the fall of the dollar.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since	
		Week Ago	Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (8/13/86)	154,290	– 48	– 1,429
New York City (8/20/86)	33,374	+ 696	+ 849
Commercial Paper (8/20/86)	322,179	+ 3,014	+50,168

Bank Loans

(Millions of Dollars)

	Commercial and Industrial Loans		
	Latest Week	Change Since	
Weekly Reporting Large Commercial Banks		Week Ago	Year Ago
Nationwide (8/13/86)	256,312	– 1,693	+ 2,830
New York City (8/20/86)	55,934	– 329	– 3,836
	Total Loans and Leases Gross Adjusted		
	Latest Week	Change Since	
		Week Ago	Year Ago
Nationwide (8/13/86)	737,951	– 1,257	+ 54,551
New York City (8/20/86)	155,159	– 1,140	+ 1,975

Financial Markets

	Friday 8/29/86	Change Since	
		Week Ago	Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	5.17%	– .31	– 2.19
180-Day Bills†	5.19	– .45	– 2.48
Longest Bills†	5.24	– .50	– 2.77
Recent Issues:			
$6^{1}/_{8}$s 8/31/88 (When Issued)	5.84	– .26	
$7^{1}/_{4}$s 6/15/90	6.32	– .18	
$7^{3}/_{8}$s 5/15/96	6.92	– .14	
$7^{1}/_{4}$s 5/15/16	7.20	– .07	
Municipals:			
Bond Buyer–20 Bond Index* (8/28/86)	6.93%	– .40	– 2.16
Blue List Total ($ Million)	$1,632	–$ 636	– $ 147
30-Day Visible Supply ($ Million)	$1,008	–$2,174	– $2,508
Total	$2,640	–$2,810	– $2,655
Corporates:			
Moody's Aa Composite (8/28/86)	9.17%	– .06	– 2.13
30-Day Visible Supply ($ Million)	$1,231	–$ 990	– $1,409
Stocks:			
Dow-Jones Averages:			
Industrials	1,898.34	+ 10.54	+ 564.33
Transportation	772.13	+ 10.38	+ 81.47
Utilities	219.15	+ 1.76	+ 59.48
65 Stocks	736.37	+ 5.91	+ 182.00
N.Y.S.E. Composite Index	145.32	+ 1.44	+ 35.93
N.Y.S.E. Avg. Daily Vol. for Week (000's)	131,102	+ 4,690	+ 49,394

* 46% Taxable equivalent 12.83%.

† Bond equivalent.

International Rates

	Friday 8/29/86	Week Ago
EURODOLLAR DEPOSIT RATES (bid)		
Overnight	5.69%	5.86%
1 month	5.75	5.86
3 month	5.56	5.86
6 month	5.56	5.81
1 year	5.62	5.94
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.15%	7.22%
Long Term (7 to 15 yrs.)	7.85	7.83

FOREIGN EXCHANGE SPOT RATES **New York Opening (8/29/86)**	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.02352	42.51
Canada	.7172	1.3943
Denmark	.1293	7.7350
France	.1486	6.7275
Germany	.4873	2.0520
Italy	.0007062	1416.00
Japan	.006417	155.83
Mexico	.001421	703.50
Netherlands	.4317	2.3165
Switzerland	.6037	1.6565
U.K.	1.4785	.6764

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The Manufacturers Hanover Financial Digest

Economic Commentary,
Selected Financial Data,
and Business Indicators

MONDAY, SEPTEMBER 15, 1986

VOLUME XXIII, NUMBER 20

Recent Business And Price Trends . . .

With autumn about to unfold in the northern hemisphere, the strength of the sun's rays may not be the only thing diminishing. According to some, so, too, are prospects for more monetary policy ease. This is because with scattered indications of a pickup in business activity emerging both here and abroad, selected precious metals prices moving sharply higher and money supply growth accelerating, some financial market participants believe that the need for, and desirability of more ease have faded—and that interest rates have nowhere to go but up.

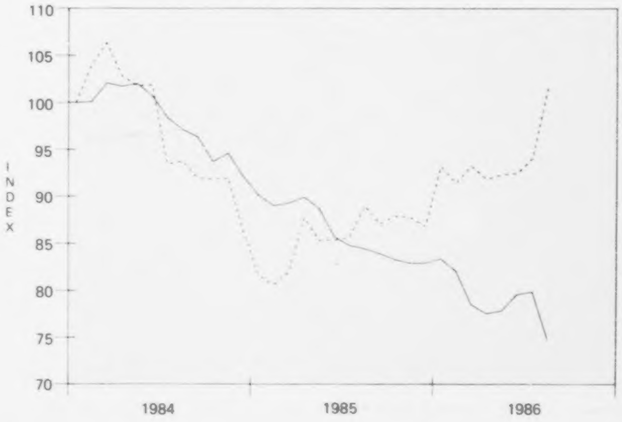
On the other hand, some argue the opposite. According to this view, the economy remains hobbled by lofty inflation-adjusted interest rates and a massive trade deficit, inflation is dormant despite the recent runup in gold, platinum and oil prices and the year-to-date growth of the broader money supply numbers, while picking up, does not yet warrant a tough Federal Reserve response. To these observers, the central bank still possesses considerable flexibility in setting the future course of monetary policy, with recent developments only diminishing the urgency with which more ease needs to be applied, not eliminating its eventual necessity.

To be sure, whatever the outcome, the thrust of monetary policy will hinge on the strength of the economy—and here the debate begins. For after being swamped by an almost nonstop string of lackluster economic statistics in recent months, something seemed to change in August. The pace of business apparently quickened as evidenced by the hefty jump in total nonfarm employment and strong month-end gains in automobile and back-to-school retail sales. Since factory orders have also begun to exhibit some vigor and the index of leading economic indicators continues to point higher, this was enough proof for some that the long-awaited economic rebound was underway, and that the need for additional monetary policy stimulation had correspondingly diminished.

. . . Have Prompted Misplaced Concerns . . .

With regard to the economy at least, this view may not be far from the mark. The areas of weakness so much in evidence in the second quarter should indeed be less of a drag on growth in subsequent quarters. As auto stocks move into better alignment with sales, inventory workdowns in this key sector will moderate; with oil prices rebounding from the depths reached in early July, the worst of the cutbacks in the "oil patch"—especially those six states which account for three quarters of domestic petroleum output—may be over. If so, then the top-line, GNP growth rate should rebound from the anemic, 0.6 percent annual rate of rise posted in the second quarter.

TUESDAY SPOT PRICE INDEX – RAW INDUSTRIALS (LINE) VS. PRICE OF GOLD (DOT) <JANUARY 1984=100>



What may be wide of the mark, however, is the view that this automatically implies that the Fed will begin to back away from its accommodative policy stance. For there are several big obstacles to a surge in economic activity, and sufficient areas of weakness to ensure that monetary policy remains quite easy. For one thing, although the pace of imports is expected to slow at some point in response to the lower-valued dollar in the foreign exchange markets, it hasn't yet. The trade deficit remains huge, restraining economic activity in general, and the manufacturing sector in particular. For another, the uncertainties associated with proposed tax reform legislation, not to mention sizable chunks of idle capacity existing throughout the economy, will continue to inhibit capital spending. While consumption and residential construction may be strong, the production side of the economy isn't—ensuring

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only moderate growth at best, and ever present fears of no growth at worst.

If undue market concern about today's business conditions is misplaced, even more so is the fear of an imminent surge in the inflation rate. As shown in the chart on page 1, the recent runup in such precious metals prices as gold and platinum has had little affect on anything else, and commodity price inflation remains nonexistent. Industrial raw materials prices, for example, have declined at a better than 13 percent annual rate during the most recent three months, and now stand some 26 percent below this cycle's, March 1984 peak. Nor do labor costs--which account for some two-thirds of all manufacturing costs—present any threat to today's tranquil price environment. Labor costs per unit of output in the manufacturing sector were virtually unchanged in the second quarter compared with the first, and over the past year have increased by only 1.3 percent. While unit labor costs in the entire private business sector advanced at twice this rate over the past year, the fact remains that price developments tend to belie the belief that a vigorous business rebound is underway and that inflation is reviving—the one-two punch which would produce a change in Fed policy.

. . . About The Stance Of Monetary Policy

What may be reviving are concerns about money growth. Although the torrid growth of the M1 money supply has been ignored all year long, a new

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 9/10/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	195.223	+ .916	+15.884
Loans to Depository Inst.	1.251	+ .280	+ .160
Float	.853	+ .339	+ .069
Total Reserve Bank Credit	213.473	+ 1.559	+19.894
Treasury Deposits with Federal Reserve Banks	3.424	+ 1.329	− .366
Currency in Circulation	202.514	+ .515	+13.147
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	159.199	− .952	+31.588
	9/10/86		
Member Bank Reserves:			
Total Reserves Held	51.484	+ .983	+ 7.895
Excess (Deficiency)	.752	− .121	+ .080
Net Free Reserves	.233	− .245	+ .284
		% Change Since Three Months Ago*	% Change Since Year Ago
Monetary Aggregates †			
M1 (9/1/86)	693.0	+ 17.6‡	+ 13.7‡
M2 (August '86)	2,722.5	+ 11.0	+ 8.2
M3 (August '86)	3,398.7	+ 10.0	+ 8.6
Domestic Nonfinancial Debt (1st Q'86)	7,033.5	+ 8.7	+ 14.2

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 9/12/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	5.20%	5.35%	5.47%
* Federal Agencies	5.43	5.46	5.60
* Municipal Notes—High Grade (46% Taxable Equivalent)	7.41	7.59	7.78
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	5.72	5.77	6.10

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	5.75%	Oct.	5.65%
15- 29 days	5.75	Nov.	5.60
30- 59 days	5.75	Dec.	5.60
60- 89 days	5.73	Jan.	5.60
90-179 days	5.65	Feb.	5.60
180-239 days	5.35	Mar.	5.55
240-270 days	5.35		

‡ Industrial Paper—Prime			
30- 89 days	5.72%	†Federal Funds	
90-120 days	5.69	Effective Rate	5.80%

‡ Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	2nd Q'86	$ 4,180	$ 4,149	$ 3,965
Gross National Product (1982 Dollars)*	2nd Q'86	$ 3,662	$ 3,656	$ 3,568
Percent Change, Annual Rate	2nd Q'86	0.6	3.8	2.3
Change in Consumer Prices*	Jul '86n	0.0%	6.0%	2.4%
Change in Producer Prices*	Aug '86n	3.6%	− 4.8%	− 3.6%
Civilian Employment (Thousands of Persons) †	Aug '86n	110,155	109,882	107,210
Unemployment as % of Civilian Labor Force †	Aug '86n	6.8%	6.9%	7.1%
Personal Income*	Jul '86	$ 3,502	$ 3,487	$ 3,315
Leading Indicators Composite Index (1967=100) †	Jul '86	179.4	177.4	169.2
Industrial Production Index (1977=100) †	Jul '86	124.1	124.2	124.1
Change in Consumer Installment Credit †	Jul '86n	$ 5.38	$ 5.39r	$ 6.79
U.S. Merchandise Trade Balance	Jul '86	−$ 18.04	−$ 13.25	−$ 13.58
Plant and Equipment Expenditures*	4th Q'86n	$383.99(a)	$380.52(a)r	$397.88r
Private Housing Starts (Thousands of Units)*	Jul '86	1,818	1,852	1,673
New Construction Expenditures*	Jul '86n	$ 376.7	$ 374.8r	$ 355.1
Total Business Inventories †	Jun '86	$ 589.0	$ 586.7	$ 580.1
Total Business Sales †	Jun '86	$ 423.6	$ 421.6	$ 418.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

wrinkle was added in recent months in light of the pickup in the growth rate of the M2 and M3 money numbers. In July, for example, M2 rose at a better than 12 percent annual rate while M3 was up at a 13½ percent annual clip; over the past three months, each has been expanding at double-digit annual rates. While some have felt for a long time that rapid money growth was the Achilles' heel in the longer-term inflation outlook, even here, the likely response is uncertain. This is because the year-to-date growth of M2 is still within the 1986 target boundaries, while that of M3 is only a shade above its upper-target boundary. Indeed, it appears a good bet that as long as a large overshoot of the growth targets for these aggregates does not materialize, the Fed will not move aggressively to rein in the growth of the money supply.

Much the same can be said for the dollar. As with faster money growth, the inflation rate dangers of a rapidly declining dollar in the foreign markets have been repeatedly cited. But not only have these fears been slow to materialize, they have yet to deter the Fed from pursuing its course of monetary ease. Nor should they in the future. In fact, dollar considerations may even hasten efforts to pull lower the lofty level of real interest rates, given the huge trade deficit and the likelihood that further dollar depreciation will be necessary if this gap is too narrow (Financial Digest—August 29, 1986). If so, what all this adds up to is that misplaced concerns notwithstanding, the Fed has several good reasons for not only keeping policy accommodative, but easing further, if and when it deems such actions appropriate.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since	
		Week Ago	Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (8/27/86)	155,344	+ 336	− 1,232
New York City (9/3/86)	32,608	− 621	− 7
Commercial Paper (9/3/86)	321,858	+ 522	+47,904

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since	
		Week Ago	Year Ago
Nationwide (8/27/86)	256,726	+ 690	+ 3,462
New York City (9/3/86)	57,755	+ 880	− 2,996

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since	
		Week Ago	Year Ago
Nationwide (8/27/86)	739,551	+ 1,976	+ 52,991
New York City (9/3/86)	160,542	+ 2,953	+ 5,887

Financial Markets

	Friday 9/12/86	Change Since	
		Week Ago	Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	5.28%	− .07	− 2.19
180-Day Bills†	5.58	+ .09	− 2.21
Longest Bills†	5.73	+ .06	− 2.45
Recent Issues:			
$6\frac{1}{8}$s 8/31/88	6.46	+ .25	
$7\frac{1}{4}$s 6/15/90	7.03	+ .57	
$7\frac{3}{8}$s 5/15/96	7.60	+ .30	
$7\frac{1}{4}$s 5/15/16	7.73	+ .19	
Municipals:			
Bond Buyer—20 Bond Index* (9/11/86)	7.15%	+ .15	− 1.92
Blue List Total ($ Million)	$1,663	+$ 74	− $ 107
30-Day Visible Supply ($ Million)	$2,016	+$1,011	− $2,378
Total	$3,759	+$1,085	− $2,485
Corporates:			
Moody's Aa Composite (9/11/86)	9.39%	+ .14	− 1.96
30-Day Visible Supply ($ Million)	$1,883	−$ 96	− $ 407
Stocks:			
Dow-Jones Averages:			
Industrials	1,758.72	−141.03	+ 423.03
Transportation	737.38	− 40.12	+ 59.83
Utilities	198.78	− 14.93	+ 39.62
65 Stocks	685.29	− 49.65	+ 133.76
N.Y.S.E. Composite Index	132.81	− 11.08	+ 23.76
N.Y.S.E. Avg. Daily Vol. for Week (000's)	182,192	+17,232	+ 93,029

* 46% Taxable equivalent 13.24%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 9/12/86	Week Ago
Overnight	5.81%	5.69%
1 month	5.88	5.81
3 month	5.88	5.75
6 month	5.88	5.75
1 year	6.13	5.88
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.58%	7.37%
Long Term (7 to 15 yrs.)	8.27	7.91

FOREIGN EXCHANGE SPOT RATES

New York Opening (9/12/86)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.02378	42.05
Canada	.7206	1.3878
Denmark	.1269	7.8825
France	.1471	6.8000
Germany	.4810	2.0788
Italy	.0006981	1432.50
Japan	.006429	155.55
Mexico	.001355	738.00
Netherlands	.4271	2.3415
Switzerland	.5876	1.7018
U.K.	1.4705	.6800

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The Manufacturers Hanover
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Economic Commentary,
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and Business Indicators

MONDAY, SEPTEMBER 29, 1986
VOLUME XXIII, NUMBER 21

Like A Patchwork Quilt . . .

Looking at a map of the individual 50 states reveals both areas of significant strength as well as pockets of paralyzing weakness. Seldom in the past have economic conditions among the states differed so dramatically. On one end of the spectrum are such states as Connecticut and Massachusetts, which have outperformed the rest of the country by almost any yardstick of economic well-being. On the other side are such oil-producing states as Louisiana and Oklahoma, which are now trailing the rest of the nation by a wide margin in terms of economic health. While these areas of weakness have so far been unable by themselves to bring the national business expansion to a halt, they have raised serious doubts about its staying power, in the absence of effective remedial actions.

One good measure of economic health is trends in employment growth. While the country as a whole increased its payroll employment by 2½ percent between June 1985 and June 1986, this average masks wide disparities between those thriving states whose economic fortunes are tied to such industries as defense and financial services, and the many heartland states where economic growth is hobbled by their dependence on declining smokestack industries and depressed agricultural and energy sectors.

. . . The States' Economies Run . . .

Connecticut is among those states that have been able to outperform the nation as a whole in its ability to generate jobs. Buoyed by higher levels of defense-related and services jobs, the state's non-agricultural employment increased by five percent during the 12 months ending in June, twice the national rate. One result of this is that the state enjoys one of the lowest jobless rates in the nation. At 3.7 percent at midyear, this was far below the 7.3 percent unemployment rate for the country as a whole at that time.

Surging employment has brought the state prosperity. The state's per person income is, for example, the second highest in the nation. At $18,089 in 1985 it is over 30 percent above the national average. It trails only Alaska's oil-boosted income, but by less than $100. The confidence in the state's economy is also reflected in an entrepreneurial boom. Over 7,200 new business incorporations took place in the first half of 1986, an increase of more than 70 percent from the first half of last year and, by far, the highest increase in the nation.

The cause of Connecticut's success appears to have been its diversification. Since the mid-1970s, after a period in which the state appeared to be losing its industrial vigor as companies and people fled to the Sunbelt states, stepped-up efforts were made to diversify the state's economy. Formerly dominated by metal-working and defense-related industries, the state has actively sought to attract such fast-growing industries as consumer goods, fiber optics, pharmaceuticals and computer software. And because of its proximity to New York City, the state also has been able to develop expertise in banking and insurance.

. . . From Bright Spots . . .

A similar success story can be found nearly 3,000 miles away—in Arizona. With its excellent year-round climate, proximity to key southwestern markets, and a fast-growing population, Arizona has become one of the major centers in the nation for the development and manufacture of high technology products. Half of the state's manufacturing employment is in such high technology industries as computers, electronic components and scientific instruments; the remaining half is in such construction-related manufacturing as stone, glass, clay, lumber and wood.

The manufacturing sector, however, accounts for less than 15 percent of the state's total nonagricultural employment. Three out of every four Arizona workers are engaged in service-related activities, which outpaced almost all other states in their generation of new jobs. Much of the strength in the service sector is related to tourism—one of the state's largest industries—and was due to strong job gains in hotels, restaurants and auto-service stations.

But, perhaps more important, Arizona owes its

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success, at least partially, to its decidedly pro-business attitude. According to a recent study, the nation's business leaders ranked Arizona's business climate the fourth most favorable among the 48 contiguous states.

. . . To Dark Patches

At the other end of the spectrum are states that must cope with the plunge in oil prices and the continuing difficulties in the farm belt. Such states as Louisiana, Texas and Oklahoma, as well as a good chunk of the Great Plains region, have all found themselves on the cutting edge of commodity price deflation.

Take, for example, Louisiana. The energy sector is the mainstay of its economy. It is the nation's second largest natural gas producer and the third largest producer of oil. Distress in the energy sector has resulted in a 26 percent drop in mining employment in the latest 12 months. The state's rig count this month was almost 60 percent below its year-ago levels. Beyond the immediate effects on the industries directly related to oil exploration, drilling and production, falling energy prices have also damaged the fiscal health of Louisiana's public sector, which clearly depends so much on energy-related revenues. It is estimated that for every dollar drop in oil prices,

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 9/24/86	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	198.711	+ 3.289	+16.967
Loans to Depository Inst.	1.094	+ .226	– .168
Float	.579	+ .061	+ .111
Total Reserve Bank Credit	217.097	+ 3.799	+20.766
Treasury Deposits with Federal Reserve Banks	7.625	+ 3.527	+ 1.024
Currency in Circulation	200.742	– .984	+13.224
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	161.580	+ 1.247	+33.538
Member Bank Reserves:	9/24/86		
Total Reserves Held	51.523	+ .092	+ 7.974
Excess (Deficiency)	.649	– .113	– .018
Net Free Reserves	.237	– .006	+ .084

Monetary Aggregates†		% Change Since Three Months Ago*	% Change Since Year Ago
M1 (9/15/86)	691.3	+ 16.4‡	+ 13.7‡
M2 (August '86)	2,723.6	+ 11.2	+ 8.3
M3 (August '86)	3,399.9	+ 10.2	+ 8.6
Domestic Nonfinancial Debt (1st Q'86)	7,033.5	+ 8.7	+ 14.2

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 9/26/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	5.27%	5.42%	5.52%
* Federal Agencies	5.45	5.57	5.64
* Municipal Notes—High Grade (46% Taxable Equivalent)	6.94	7.03	7.31
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	5.82	5.82	6.05

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	5.80%	Oct.	5.75%
15- 29 days	5.75	Nov.	5.75
30- 59 days	5.73	Dec.	5.65
60- 89 days	5.45	Jan.	5.65
90-179 days	5.30	Feb.	5.65
180-239 days	5.15	Mar.	5.65
240-270 days	5.15		

‡ Industrial Paper—Prime			
30- 89 days	5.82%	† Federal Funds	
90-120 days	5.78	Effective Rate	5.85%

‡ Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

		Latest Period or End of Period	Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	2nd Q'86	$ 4,176r	$ 4,149	$ 3,965
Gross National Product (1982 Dollars)*	2nd Q'86	$ 3,662r	$ 3,656	$ 3,568
Percent Change, Annual Rate	2nd Q'86	0.6r	3.8	2.3
Change in Consumer Prices*	Aug '86n	2.4%	0.0%	2.4%
Change in Producer Prices*	Aug '86	3.6%	– 4.8%	– 3.6%
Civilian Employment (Thousands of Persons)†	Aug '86	110,155	109,882	107,210
Unemployment as % of Civilian Labor Force†	Aug '86	6.8%	6.9%	7.1%
Personal Income*	Aug '86n	$ 3,505	$ 3,493r	$ 3,321
Leading Indicators Composite Index (1967=100)†	Jul '86	179.4	177.4	169.2
Industrial Production Index (1977=100) †	Aug '86n	124.8	124.6r	124.4r
Change in Consumer Installment Credit †	Jul '86	$ 5.38	$ 5.39	$ 6.79
U.S. Merchandise Trade Balance	Jul '86	–$ 18.04	–$ 13.25	–$ 13.58
Plant and Equipment Expenditures*	4th Q'86	$383.99(a)	$380.52(a)	$397.88
Private Housing Starts (Thousands of Units)*	Aug '86n	1,822	1,815r	1,737
New Construction Expenditures*	Jul '86	$ 376.7	$ 374.8	$ 355.1
Total Business Inventories †	Jul '86n	$ 591.3	$ 588.9r	$ 580.4r
Total Business Sales †	Jul '86n	$ 428.5	$ 425.5r	$ 421.6r

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

Louisiana loses $500 million in taxes.

The weakness in Louisiana's economy is reflected in its pattern of income and spending growth. The state's personal income growth has been consistently below that of the nation as a whole. While personal income for the country as a whole rose by almost five percent in the last year, Louisiana's income remained stagnant. Not surprisingly, the state's retail sales in the first six months declined 1.6 percent, one of only two states—the other was Texas which finds itself in its own energy-related slump—to post declines of more than one percent among the nation's 19 largest states.

Louisiana's economic hardships are unusually severe because during the energy-boom days the state took few steps to diversify its economy. As a result, the state is extremely sensitive to the changes in world energy markets, government energy policy and the investment decisions of a relatively few energy and chemical companies. Before 1982, this did not seem to matter, and the state's booming economy attracted workers from other areas of the country, who fueled economic growth as they bought homes, cars and other goods and services. Now, a contracting economy is causing a reverse flow of people, reinforcing this state's economic contraction.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since	
		Week Ago	Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (9/10/86)	154,238	+ 495	– 2,317
New York City (9/17/86)	32,927	+ 259	+ 523
Commercial Paper (9/17/86)	329,338	+ 6,954	+53,175

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since	
		Week Ago	Year Ago
Nationwide (9/10/86)	256,919	– 1,812	+ 2,483
New York City (9/17/86)	57,477	+ 440	– 3,359

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since	
		Week Ago	Year Ago
Nationwide (9/10/86)	743,173	– 4,171	+ 50,976
New York City (9/17/86)	160,934	+ 2,130	+ 6,625

Financial Markets

	Friday 9/26/86	Change Since	
		Week Ago	Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	5.35%	– .02	– 1.92
180-Day Bills†	5.57	– .08	– 1.83
Longest Bills†	5.77	– .04	– 2.18
Recent Issues:			
$6\frac{3}{8}$s 9/30/88 (When Issued)	6.35	NA	
$6\frac{3}{4}$s 9/30/90 (When Issued)	6.87	NA	
$7\frac{3}{8}$s 5/15/96	7.44	– .24	
$7\frac{1}{4}$s 5/16/16	7.61	– .24	
Municipals:			
Bond Buyer–20 Bond Index* (9/25/86)	7.15%	+ .01	– 2.23
Blue List Total ($ Million)	$1,647	+ $ 52	– $ 311
30-Day Visible Supply ($ Million)	$2,055	+ $215	– $1,731
Total	$3,702	+ $267	– $2,042
Corporates:			
Moody's Aa Composite (9/25/86)	9.40%	– .03	– 2.09
30-Day Visible Supply ($ Million)	$3,706	– $512	+ $ 708
Stocks:			
Dow-Jones Averages:			
Industrials	1,769.69	+ 7.18	+ 448.90
Transportation	784.25	+ 4.12	+ 140.64
Utilities	201.75	+ .66	+ 51.67
65 Stocks	701.06	+ 2.98	+ 165.43
N.Y.S.E. Composite Index	133.94	+ .45	+ 29.12
N.Y.S.E. Avg. Daily Vol. for Week (000's)	128,668	–14,120	+ 28,448

* 46% Taxable equivalent 13.24%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 9/26/86	Week Ago
Overnight	5.81%	5.75%
1 month	6.00	6.06
3 month	6.00	6.06
6 month	6.00	6.06
1 year	6.13	6.25
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.57%	7.49%
Long Term (7 to 15 yrs.)	8.35	8.26

FOREIGN EXCHANGE SPOT RATES

New York Opening (9/26/86)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.02362	42.33
Canada	.7195	1.3899
Denmark	.1292	7.7395
France	.1495	6.6855
Germany	.4898	2.0415
Italy	.0007084	1411.50
Japan	.006482	154.25
Mexico	.001325	754.50
Netherlands	.4335	2.3070
Switzerland	.6045	1.6542
U.K.	1.4367	.6960

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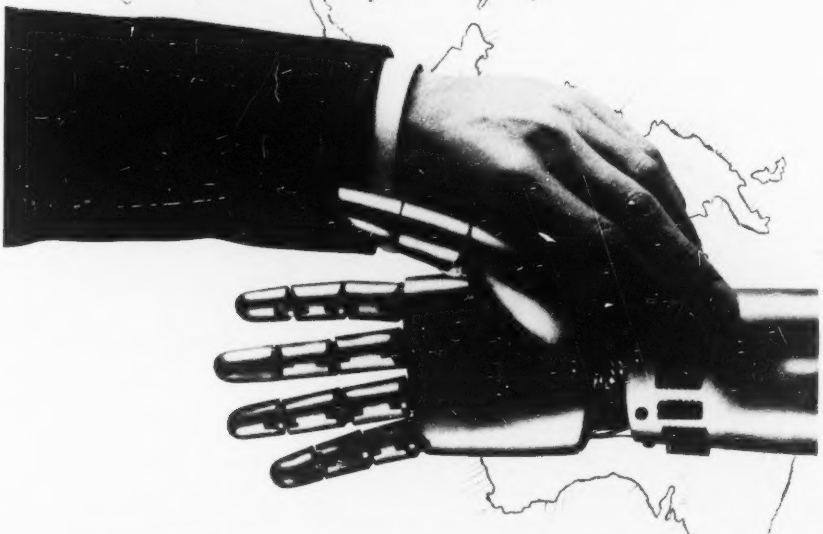

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The Manufacturers Hanover Financial Digest

Economic Commentary,
Selected Financial Data,
and Business Indicators

FRIDAY, OCTOBER 10, 1986 VOLUME XXIII, NUMBER 22

Some Bright Spots In Manufacturing . . .

At first glance the manufacturing sector of the U.S. economy still appears to be mired in the recessionary swamp which it first tumbled into in the middle of 1984, beset by a flood of imports, flat exports, low profits and declining manufacturing employment. Factory orders plummeted 1.4 percent in August and manufacturing employment fell by 38,000 jobs in September after a meager uptick of 1,000 jobs in August. Capacity utilization in America's factories is under 80 percent, seemingly discouraging capital investment.

Yet beneath this gloomy facade there are reasons for some guarded optimism about the manufacturing sector. For example, the announcement in early September that American businesses were cutting back even further on their capital spending plans than was previously anticipated was dismal news indeed—but only superficially. The 1986 slowdown of plant and equipment spending can almost entirely be blamed on the energy sector. If petroleum refiners are excluded, planned expenditures for 1986 hold steady compared with 1985. What is more, if mining—the other major component of the energy sector—is also excluded, total 1986 plant and equipment spending plans reverse direction from a 1.9 percent slide to a 1.3 percent rise. In fact, in the manufacturing sector, eight of 16 industries surveyed by the U.S. Department of Commerce are presently boosting their 1986 capital budgets. Increases of almost 12 percent over last year are anticipated in the aircraft and fabricated metals industries, reflecting the brighter picture for transportation and construction. Chemical, rubber and paper manufacturers also are planning to spend more on plant and equipment this year than last.

Yet another development that suggests improvement is the recent firming of industrial materials prices. Since late August the Commodity Research Bureau's index of raw industrials has risen eight percent. Led by a 44 percent rise in cotton prices, prices of eight of the 13 industrial raw materials surveyed rose, while two stayed flat and three fell. The rise in prices for these industrial inputs points up an improving balance between supply and demand and is a reversal of the sharp decline in raw materials prices which began in early 1984.

. . . Where Jobs Are Up . . .

A closer look at the otherwise gloomy manufacturing employment figures also reveals pockets of strength. Although manufacturing employment has fallen by 0.6 percent over the past twelve months, there are some manufacturing industries in which employment has risen over the same period. Of the 20 principal manufacturing industry sectors, nine have had year-over-year gains in employment. Among the more important, employment has increased in the lumber industry, printing and publishing, textiles, food processing, rubber, paper, furniture and transportation equipment industries. While some of the gains have been modest in terms of the number of workers involved, they do represent areas of rising economic activity, or else these industries would not be adding to payrolls.

The textile, lumber, and furniture industries, as well as the stone, clay and glass industry (which has also posted a small rise in employment) have benefited from the strong level of housing starts so far this year and the increase in residential expenditures on additions and alterations. By contrast, the gain in employment in the transportation equipment industry as a whole masks two very different scenarios within the industry. While employment in the aircraft industry rose a strong 5.8 percent over the past twelve months, the number of motor vehicle and parts workers fell five percent. Not only did strong defense spending benefit the aircraft industry but global demand for commercial aircraft to replace aging fleets added a beneficial fillip to both domestic sales and exports. The auto industry on the other hand, in spite of a good sales year, continues to suffer from powerful import competition.

Interestingly, textiles, one of the industries often cited as particularly subject to import competition, reports a 1.7 percent gain in employment in the past year. But as late as May of this year, employment was soft. However, plant restructurings, company mergers and consolidations, a more efficient use of

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resources and record levels of capital spending in the last three years have left this industry leaner and more efficient, although imports of textile and apparel products remain a major problem.

. . . And Profits, Too

Another way to measure improvement in the manufacturing sector is growing profits. It also provides another dimension for the more capital-intensive industries. Several industries have shown a marked upturn over the past year, some of which are emerging from very low profit levels of the past few years. A major contributor to improved profits has been the consolidation process which has resulted in mergers, acquisitions, or bankruptcies of marginal producers, leaving the market with fewer, more efficient firms. For example, the textile industry, whose after-tax profits doubled between the first half of 1985 and the same period this year, has experienced over 250 mill closings since 1980.

Yet another beneficiary of consolidation is the rubber and plastics industry which has also profited from declining petroleum prices, an important raw material for this industry. This industry's after-tax profits in the first half of 1986 were almost 22 percent higher than for the same period in 1985. Meanwhile, the stone, clay and glass industry sector whose net profits jumped 30 percent from last year's first six months to this year's, is a major supplier to the construction industry which is having one of its best years in recent history.

Chemical companies (including producers of

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending	$ Change Since	
Reserve Bank Credit	10/8/86	Week Ago	Year Ago
U.S. Gov'ts and Agencies Owned Outright & RPs	195.043	– 3.691	+17.057
Loans to Depository Inst.	.863	– .077	– .486
Float	.479	– .054	– .376
Total Reserve Bank Credit	212.923	– 4.411	+19.579
Treasury Deposits with Federal Reserve Banks	3.424	– 5.206	+ .515
Currency in Circulation	201.610	+ 1.288	+12.846
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	162.954	+ .219	+37.176
Member Bank Reserves:	10/8/86		
Total Reserves Held	51.767	+ .204	+ 7.540
Excess (Deficiency)	.849	+ .128	+ .202
Net Free Reserves	.485	+ .176	+ .606
		% Change Since	
Monetary Aggregates †		Three Months Ago*	Year Ago
M1 (9/29/86)	693.6	+ 15.9‡	+ 13.3‡
M2 (August '86)	2,723.7	+ 11.2	+ 8.3
M3 (August '86)	3,399.8	+ 10.2	+ 8.6
Domestic Nonfinancial Debt (2nd Q'86)	7,181.0	+ 11.5	+ 13.1

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 10/10/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	5.07%	5.12%	5.30%
* Federal Agencies	5.31	5.36	5.44
* Municipal Notes–High Grade (46% Taxable Equivalent)	6.02	6.02	6.30
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market–Prime	5.64	5.62	5.75

‡ Finance Company Paper–Prime		‡* Bankers' Acceptances	
5- 14 days	5.65%	Nov.	5.70%
15- 29 days	5.68	Dec.	5.60
30- 59 days	5.68	Jan.	5.53
60- 89 days	5.65	Feb.	5.50
90-179 days	5.62	Mar.	5.48
180-239 days	5.55	Apr.	5.45
240-270 days	5.55		

‡ Industrial Paper–Prime		† Federal Funds	
30- 89 days	5.66%		
90-120 days	5.67	Effective Rate	5.70%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	2nd Q'86	$ 4,176	$ 4,149	$ 3,965
Gross National Product (1982 Dollars)*	2nd Q'86	$ 3,662	$ 3,656	$ 3,568
Percent Change, Annual Rate	2nd Q'86	0.6	3.8	2.3
Change in Consumer Prices*	Aug '86	2.4%	0.0%	2.4%
Change in Producer Prices*	Sep '86n	4.8%	3.6%	– 7.2%
Civilian Employment (Thousands of Persons) †	Sep '86n	109,891	110,155	107,519
Unemployment as % of Civilian Labor Force†	Sep '86n	7.0%	6.8%	7.1%
Personal Income*	Aug '86	$ 3,505	$ 3,493	$ 3,321
Leading Indicators Composite Index (1967=100)†	Aug '86n	179.1	179.5r	169.8
Industrial Production Index (1977=100) †	Aug '86	124.8	124.6	124.4
Change in Consumer Installment Credit †	Aug '86n	$ 3.74	$ 5.56r	$ 6.05r
U.S. Merchandise Trade Balance	Aug '86n	–$ 13.32	–$ 16.06r	–$ 12.89
Plant and Equipment Expenditures*	4th Q'86	$383.99(a)	$380.52(a)	$397.88
Private Housing Starts (Thousands of Units)*	Aug '86	1,822	1,815	1,737
New Construction Expenditures*	Aug '86n	$ 382.2	$ 378.1r	$ 353.3
Total Business Inventories †	Jul '86	$. 591.3	$ 588.9	$ 580.4
Total Business Sales †	Jul '86	$ 428.5	$ 425.5	$ 421.6

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

drugs and pharmaceuticals) have had an almost five percent improvement in after-tax profits between the first halves of last year and this year. In the same period the fabricated metals industry and the electrical and electronic industry have seen their profits rise by over seven percent. And several industries have continued to be bright spots in the generally poor American industrial scene due to their acknowledged global leadership. These are primarily high technology industries such as aircraft and computers. Although these industries have not necessarily shown the highest growth rates in the last year, they remain among the stars of U.S. industry.

A perusal of the list of industries which have shown recent improvement in employment levels and/or profits suggests some reasons why these particular industries may have grown. In most of the cases their products find their markets in the service or construction sectors of the economy or directly in retail sales—all of which are sources of strength in the present U.S. economic environment. In several cases these industries produce goods which for a variety of economic or regulatory reasons are less susceptible to import competition. Rising employment, higher disposable income, low inflation rates, declining interest rates and prospects for lower individual taxes next year have all contributed to rising demand for housing, transportation and improved health care, which in turn, has benefited the manufacturing industries that serve these sectors.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (9/24/86)	154,721	+ 932	− 3,696
New York City (10/1/86)	33,727	+ 773	+ 782
Commercial Paper (10/1/86)	328,280	− 990	+49,157

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (9/24/86)	257,130	− 1,519	+ 2,613
New York City (10/1/86)	58,271	+ 1,274	− 2,331

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (9/24/86)	746,103	− 3,587	+ 53,564
New York City (10/1/86)	165,409	+ 4,416	+ 10,911

Financial Markets

	Friday 10/10/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	5.18%	− .03	− 2.27
180-Day Bills†	5.30	− .06	− 2.42
Longest Bills†	5.54	− .03	− 2.50
Recent Issues:			
$6^{3}/_{8}$s 9/30/88	6.12	+ .02	
$6^{3}/_{4}$s 9/30/90	6.63	−0−	
$7^{3}/_{8}$s 5/15/96	7.33	+ .04	
$7^{1}/_{4}$s 5/16/16	7.64	+ .12	
Municipals:			
Bond Buyer—20 Bond Index* (10/9/86)	7.06%	− .13	− 2.19
Blue List Total ($ Million)	$1,518	−$ 180	− $ 189
30-Day Visible Supply ($ Million)	$1,937	−$ 100	− $2,646
Total	$3,455	−$ 280	− $2,835
Corporates:			
Moody's Aa Composite (10/9/86)	9.31%	− .04	− 2.20
30-Day Visible Supply ($ Million)	$5,795	+$2,872	+ $3,360
Stocks:			
Dow-Jones Averages:			
Industrials	1,793.17	+ 18.99	+ 453.23
Transportation	824 13	+ 12.25	+ 176.66
Utilities	198.19	− 1.44	+ 44.10
65 Stocks	714.27	+ 6.52	− 171.16
N.Y.S.E. Composite Index	135.70	+ .89	+ 29.14
N.Y.S.E. Avg. Daily Vol. for Week (000's)	122,698	− 5,338	+ 26,652

* 46% Taxable equivalent 13.07%.

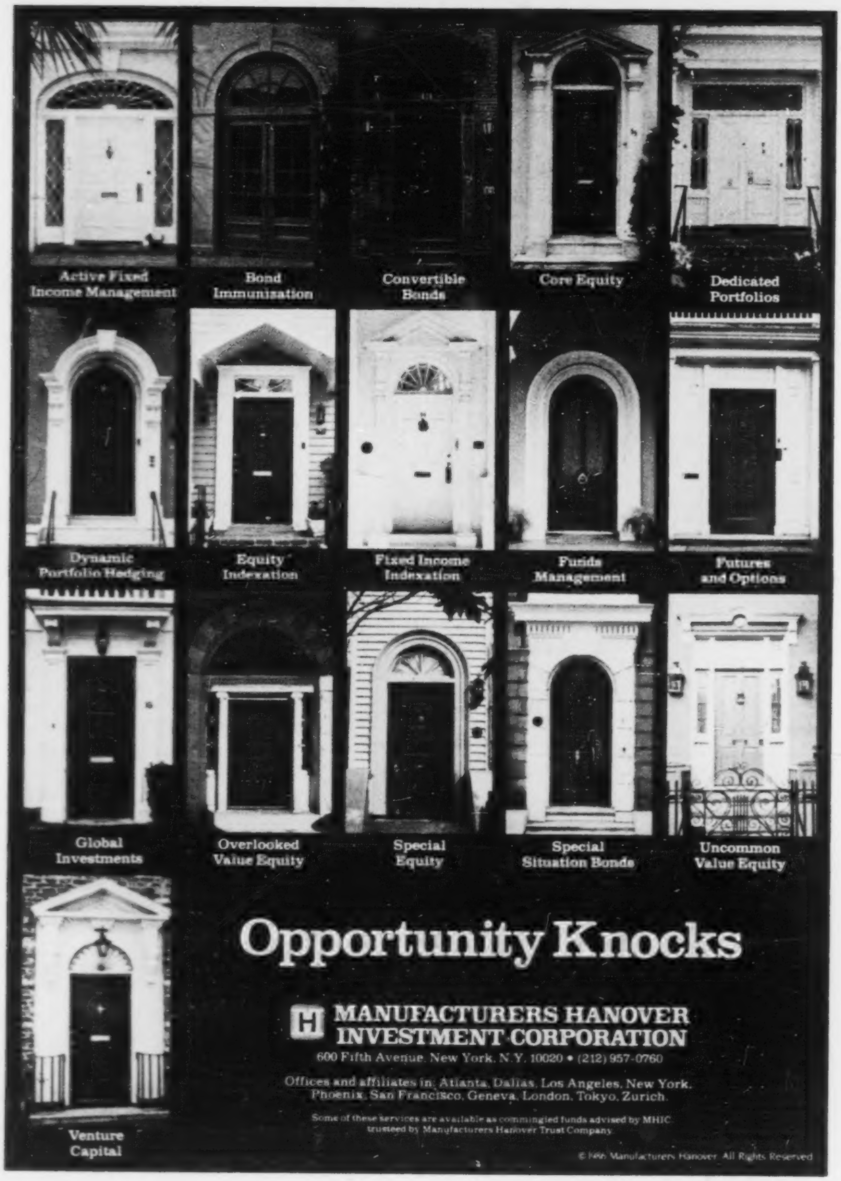
† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 10/10/86	Week Ago
Overnight	5.75%	5.75%
1 month	5.75	5.86
3 month	5.75	5.86
6 month	5.75	5.86
1 year	5.86	5.94
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.34%	7.57%
Long Term (7 to 15 yrs.)	8.19	8.35

FOREIGN EXCHANGE SPOT RATES

New York Opening (10/10/86)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.02405	41.58
Canada	.7216	1.3858
Denmark	.1327	7.5350
France	.1524	6.5625
Germany	.4991	2.0035
Italy	.0007212	1386.50
Japan	.006443	155.20
Mexico	.001270	787.50
Netherlands	.4418	2.2635
Switzerland	.6124	1.6330
U.K.	1.4285	.7000



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MONDAY, OCTOBER 27, 1986 VOLUME XXIII, NUMBER 23

The Consumer . . .

Consumer spending has long been the dominant force behind the current business expansion, and this year is no exception. Over the past three quarters, growth in personal consumption expenditures has counteracted the weaknesses in other sectors of the economy. For example, while the inflation-adjusted gross national product increased at an annual rate of only 2.2 percent in the January-September period, real personal consumption expenditures climbed by a healthier 5.6 percent annual rate. In the third quarter of 1986, real consumer spending bolted upward at a 7.2 percent clip—three times as fast as the 2.4 percent rise posted by the real GNP. This disparity has raised concerns in some quarters that consumers may be living beyond their means. Indeed, if they are financially tapped out, any retrenchment in their spending could put a damper on this business expansion, which is now concluding its fourth year.

At first glance, consumers do appear to be overextended. Since spending has risen faster than after-tax income so far this year, consumers have dipped into their savings or resorted to buying on credit. As a result, the savings rate—savings as a percent of disposable income—is now 1.9 percent, the lowest rate in at least 35 years, while consumer credit outstanding compared with take-home income has reached a record 19.3 percent. These aggregate figures, however, mask a more positive picture of consumer finances.

For example, the savings rate number most often quoted may be somewhat misleading because of the methodology used to calculate the level of savings. The Commerce Department estimates disposable personal income and personal consumption expenditures and derives savings as the difference between the two. This method, however, does not make any adjustment to spending when purchases are made on credit. For example, in computing personal outlays, the total dollar amount of new cars sold is included, although only 25 percent of all new cars sold are paid in full at the time of the purchase. The other 75 percent are bought on credit.

This factor becomes important in light of the strong sales of new cars in August and September. The cut-rate financing offered by automakers to clear out high inventories of unsold 1986 models spurred an extraordinary jump in sales in August and September. If these unusual increases in car sales were excluded, the savings rates in August and September would rise to a more typical 3.8 percent and 3.7 percent, respectively. Moreover, if the dollar amount spent on new cars that was obtained through financing is taken out of consumption expenditures, the savings rate for both months would jump even higher.

. . . Appears Still Able . . .

In the case of consumer debt, in the past the upward climb of the ratio of outstanding installment debt to disposable income might have suggested that consumers were becoming overextended. Not this time. This is because much of the debt accumulated in recent years has been taken on by those high-income households which are probably best able to service it. According to Federal Reserve estimates, almost 50 percent of consumer installment debt outstanding is owed by households in the top income quintile. This proportion represents a substantial increase from 1977 when the richest households held 36 percent of such debt, and from 1970 when they accounted for only 22 percent. Add to this the fact that credit cards are used increasingly for convenience rather than for borrowing, with the holder often paying off the entire balance each billing period, and the actual burden of outstanding debt diminishes even further.

Already, consumers are cutting back on credit use without any dampening effects on their purchases. So far this year, consumers have taken on less than $42 billion in installment loans compared with $52.5 billion during the same period of last year. This was the smallest such increase in three years. Yet at the same time, retail sales rose 8.8 percent, compared with 7.5 percent last year. In August alone, the rise in consumer credit was a modest $3.7 billion. While auto credit accounted for two-thirds of this increase, its growth slowed to a mere $2.5 billion compared with an average increase of $3.5 billion in the preceding three months. This is somewhat puzzling in view of the fact that August car sales soared in response to new incentives

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offered by automakers. It may indicate that many buyers either opted for cash rebates which reduced the amount of credit needed, or took the higher interest rate loans which allowed them more time to repay.

. . . To Keep The Expansion Going

Although the total level of indebtedness is certainly a consideration, it is the monthly repayments of such obligations in relation to disposable income which determine the true burden on consumers. Longer loan payback periods, lower interest rates, and growth in overall household assets have contributed to easing the burden of monthly installment payments, despite the very rapid growth in total installment debt over the last several years. According to a new study by the Federal Reserve, the ratio of consumer installment debt to disposable income was 24 percent higher in the first quarter of this year than in the first quarter of 1975. However, the ratio of debt service payments to disposable income was four percent lower.

The lengthening of maturities on many types of loans since 1975 accounts for much of this difference between the growth patterns of consumer installment debt and debt service payments. For example, the average maturity of new car loans issued by finance companies increased from 38 months in 1975 to 52 months in 1985. Clearly, an increase in maturity can decrease the scheduled monthly repayments of principal, even as it raises aggregate debt outstanding. If maturities had not increased, the consumer installment debt ratio

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 10/22/86	$ Change Since	
		Week Ago	Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	197.934	+ 2.269	+18.567
Loans to Depository Inst.	.888	+ .235	− .413
Float	.601	− .145	− .268
Total Reserve Bank Credit	216.068	+ 2.323	+20.500
Treasury Deposits with Federal Reserve Banks	3.552	+ .851	− .098
Currency in Circulation	202.763	− .294	+13.362
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	164.010	− .109	+41.101
	10/22/86		
Member Bank Reserves:			
Total Reserves Held	52.581	+ .814	+ 8.311
Excess (Deficiency)	.775	− .074	− .018
Net Free Reserves	.492	− .188	+ .169

		% Change Since	
Monetary Aggregates†		Three Months Ago*	Year Ago
M1 (10/13/86)	696.5	+ 15.6‡	+ 13.7‡
M2 (September '86)	2,741.3	+ 10.6	+ 8.4
M3 (September '86)	3,425.2	+ 10.3	+ 8.7
Domestic Nonfinancial Debt (2nd Q'86)	7,181.0	+ 11.5	+ 13.1

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 10/24/86	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	5.30%	5.38%	5.48%
* Federal Agencies	5.45	5.51	5.60
* Municipal Notes—High Grade (46% Taxable Equivalent)	5.74	6.02	7.04
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	5.75	5.75	5.90

‡ Finance Company Paper—Prime		‡* Bankers' Acceptances	
5- 14 days	5.50%	Nov.	5.70%
15- 29 days	5.65	Dec.	5.65
30- 59 days	5.75	Jan.	5.65
60- 89 days	5.70	Feb.	5.61
90-179 days	5.70	Mar.	5.60
180-239 days	5.60	Apr.	5.58
240-270 days	5.60		

‡ Industrial Paper—Prime			
30- 89 days	5.73%	† Federal Funds	
90-120 days	5.67	Effective Rate	5.80%

‡Discount basis. * Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'86n	$ 4,234	$ 4,176	$ 4,031
Gross National Product (1982 Dollars)*	3rd Q'86n	$ 3,683	$ 3,661	$ 3,604
Percent Change, Annual Rate	3rd Q'86n	2.4	0.6	4.1
Change in Consumer Prices*	Sep '86n	3.6%	2.4%	2.4%
Change in Producer Prices*	Sep '86	4.8%	3.6%	− 7.2%
Civilian Employment (Thousands of Persons)†	Sep '86	109,891	110,155	107,519
Unemployment as % of Civilian Labor Force†	Sep '86	7.0%	6.8%	7.1%
Personal Income*	Sep '86n	$ 3,512	$ 3,500r	$ 3,334
Leading Indicators Composite Index (1967=100)†	Aug '86	179.1	179.5	169.8
Industrial Production Index (1977=100) †	Sep '86n	125.3	125.1r	124.3
Change in Consumer Installment Credit †	Aug '86	$ 3.74	$ 5.56	$ 6.05
U.S. Merchandise Trade Balance	Aug '86	−$ 13.32	−$ 16.06	−$ 12.89
Plant and Equipment Expenditures*	4th Q'86	$383.99(a)	$380.52(a)	$397.88
Private Housing Starts (Thousands of Units)*	Sep '86n	1,680	1,818r	1,653
New Construction Expenditures*	Aug '86	$ 382.2	$ 378.1	$ 353.3
Total Business Inventories †	Aug '86n	$ 591.9	$ 591.9r	$ 579.5
Total Business Sales †	Aug '86n	$ 429.1	$ 427.5r	$ 428.2

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

would have risen only eight percent between the first quarters of 1975 and 1986 rather than the actual 24 percent, and the debt service payment ratio would have increased three percent instead of falling four percent.

Households' wealth is also a crucial determinant of consumption patterns. In the first half of this year, household financial assets, which include demand deposits, savings accounts, and stocks and bonds increased at a seasonally adjusted annual rate of 17.5 percent. At the same time, household liabilities, which include mortgages as well as installment debt and other outstanding loans, rose at only an 8.3 percent annual rate. By better managing their funds, consumers have enhanced their balance sheets. Households now hold $3.35 in financial assets for each dollar of their debt outstanding, the highest such ratio in ten years.

More good news comes from the inflation front. In the past 12 months, consumer prices rose a modest 1.7 percent, enabling consumers to enjoy increased buying power from their take-home pay. These modest increases in prices also helped to push the discomfort index, which measures the sum of unemployment and inflation rates, down to 8.5 percent in the third quarter—the lowest in more than 17 years. Thus, it is not surprising that consumer attitudes are brightening just in time for the Holiday shopping season. The Conference Board reported that consumer confidence, which sagged during the summer months, moved higher in September.

Short Term Paper Outstanding

(Millions of Dollars)

	Latest Week	Change Since Week Ago	Change Since Year Ago
Time Deposits of $100,000 or more Weekly Reporting Banks			
Nationwide (10/8/86)	153,764	+ 48	– 5,325
New York City (10/15/86)	33,487	+ 58	+33,456
Commercial Paper (10/15/86)	330,667	+ 810	+45,993

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (10/8/86)	258,906	– 737	+ 4,463
New York City (10/15/86)	58,850	+ 512	+ 59,947

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (10/8/86)	747,304	– 6,457	+ 49,919
New York City (10/15/86)	163,182	+ 1,485	+ 152,424

Financial Markets

	Friday 10/24/86	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	5.38%	+ .05	– 1.85
180-Day Bills†	5.53	+ .04	– 1.88
Longest Bills†	5.75	+ .08	– 1.74
Recent Issues:			
6 3/8s 10/31/88 (When Issued)	6.31	+ .07	
6 3/4s 9/30/90	6.55	– .22	
7 3/8s 5/15/96	7.42	– .12	
7 1/4s 5/16/16	7.74	– .09	
Municipals:			
Bond Buyer–20 Bond Index* (10/23/86)	7.11%	+ .03	– 1.84
Blue List Total ($ Million)	$1,568	–$ 11	– $ 138
30-Day Visible Supply ($ Million)	$2,094	–$ 595	– $2,267
Total	$3,662	–$ 606	– $2,405
Corporates:			
Moody's Aa Composite (10/23/86)	9.33%	– .04	– 2.07
30-Day Visible Supply ($ Million)	$5,242	+$1,687	+ $ 881
Stocks:			
Dow-Jones Averages:			
Industrials	1,832.26	– 4.78	+ 475.74
Transportation	825.00	+ 1.12	+ 175.42
Utilities	202.27	+ 1.21	+ 43.11
65 Stocks	725.43	– .12	+ 175.30
N.Y.S.E. Composite Index	137.27	– .21	+ 28.91
N.Y.S.E. Avg. Daily Vol. for Week (000's)	127,032	+ 7,602	+ 16,220

* 46% Taxable equivalent 13.17%.

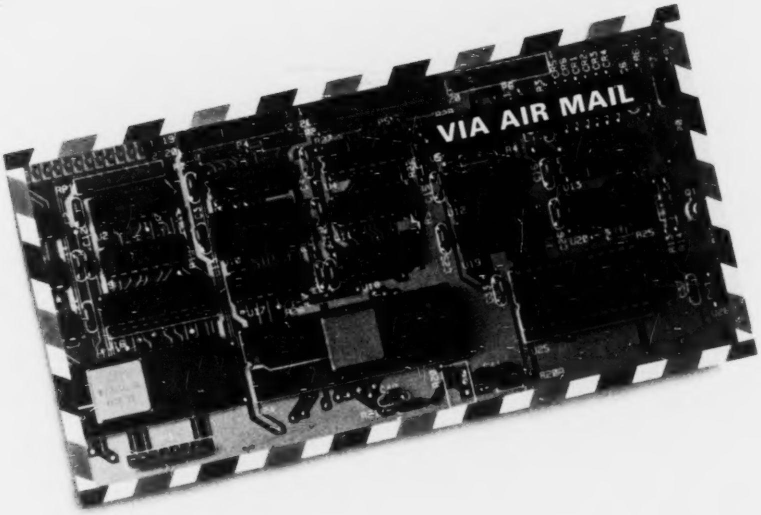
† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 10/24/86	Week Ago
Overnight	5.75%	5.75%
1 month	5.94	5.88
3 month	5.94	5.88
6 month	5.94	5.88
1 year	6.06	6.06
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 to 7 yrs.)	7.50%	7.34%
Long Term (7 to 15 yrs.)	8.44	8.22

FOREIGN EXCHANGE SPOT RATES

New York Opening (10/24/86)	**U.S. $ Equivalent**	**Currency Per U.S. $**
Belgium	.02388	41.88
Canada	.7199	1.3890
Denmark	.1313	7.6175
France	.1513	6.6100
Germany	.4948	2.0210
Italy	.0007153	1398.00
Japan	.006211	161.00
Mexico	.001242	805.00
Netherlands	.4381	2.2825
Switzerland	.5993	1.6685
U.K.	1.4145	.7070



The Letter of Credit Comes of Age.

For generations, there was not much change in the way importers handled their L/C's. From sending an application to checking on a transaction's status, the process of paperwork and phone calls could take days to complete.

Now Manufacturers Hanover Trust is bringing the L/C into the electronic age with the Electronic Letter of Credit Service. Allowing you to prepare and transmit letter of credit transactions directly to us via Personal Computer. And obtain up-to-the-instant computer reports on your letter of credit activity. Swiftly. Accurately. Securely.

With our Electronic Letter of Credit Service your instructions are acknowledged in seconds, and processed without delay. Opening the way to an early delivery of your shipment—and a savings in time and money.

You can track the status of your L/C's and acceptances through our on-line inquiry capability. A unique feature of which allows you to generate reports in standard formats or to design your own.

Add to all of this the assurance that our dedicated team of trade professionals stands ready to give you prompt answers to all your questions.

So put some byte into your L/C with our Electronic Letter of Credit Service. It's one of a number of products that is opening up a new age in banking.

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